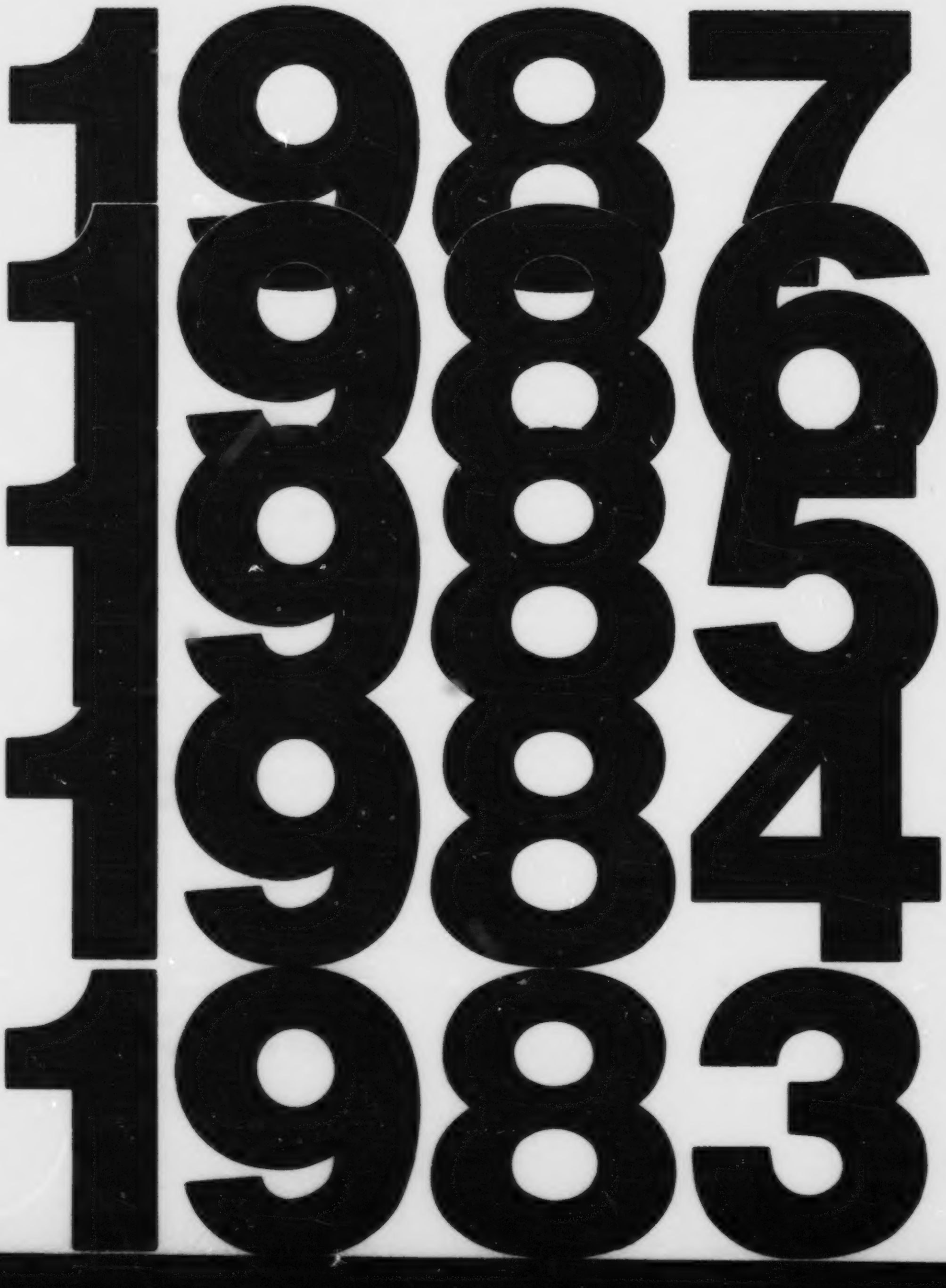
ERRATUM

P. 109: add "arrangements." at the end of the first paragraph in the left-hand column.

On the Mend

On the Mend

Economic Council of Canada
Twentieth Annual Review, 1983


1987
1986
1985
1984
1983

©Minister of Supply and Services Canada 1983

Available in Canada through

Authorized Bookstore Agents
and other bookstores

or by mail from

Canadian Government Publishing Centre
Supply and Services Canada
Ottawa, Canada, K1A 0S9

Catalogue No. EC 21-1/1983E
ISBN 0-660-11442-9

Canada: $5.95
Other countries: $7.15

Price subject to change without notice

L'Exposé annuel est aussi disponible en français.

Contents

Members of the Economic Council of Canada vii

Preface ix

1 From Then to Now 1
- In Retrospect 1
- Taking Stock 7
- Bearing the Costs 11
- From Now Till Then 14

2 The Trading Scene 17
- The Broader Context 17
- The Changing Trade Picture 18
- The North American Nexus 19
  - The Automotive Trade 21
  - Other Trading Links 22
  - Intracorporate Trade 22
- Beyond North America 23
- The "Invisible" Trade 26
- Tariff Cuts and Nontariff Barriers 27
- Other Trading Issues 29
- International Financial Issues 30
  - The Foreign-Debt Crisis 30
  - Currency Developments 32
  - Investment 32
- Possible Fresh Initiatives 33
- A New Era for Trade Negotiations 34

3 Recession and Recovery 37
- The Recession Abroad 37
- The Recession in Canada 40
  - The Effect on Unemployment 40
  - The Effect on Inflation 42
  - The Effect on Government Balances 42
  - The Effect on the Current Account Balance 43
- Looking Ahead 43
  - The External Environment 44
  - Energy Supply, Demand, and Price 45
  - Fiscal and Monetary Policy 47
  - Highlights of the Base Case 48

- Sources of Uncertainty 49
- Variations to the Base Case 50
- Some Critical Issues 53
  - Is the Federal Deficit Cyclical or Structural? 53
  - The Real Rate of Interest 56
  - What Can Fiscal and Monetary Policies Do? 57

4 Social Concerns **59**

- The Unemployment Insurance Safety Net 60
- Labour Market Policy 62
  - The Past Record 62
  - Recent Initiatives 63
    - UI-Based Work-Sharing Program 63
    - UI-Based Job Creation Programs 63
    - NEED and Canada Works 64
- Social Assistance 65
  - Recent Caseload Increases 66
  - Program Changes 67
  - The Welfare-to-Work Transition 68
- An International Comparison 70
- Housing Assistance 73
- Conclusion 79

5 Women and Work: Opportunity for Choice **81**

- Labour Market Participation 82
- Education and Training 84
- Earnings 86
- Special Problems 90
  - Single Parents 90
  - Native Women 90
  - Women and Pensions 91
- Conclusion 93

6 Conclusions and Recommendations **95**

- Our Targets 96
  - Productivity and Employment Growth 98
  - Inflation 99
  - Domestic Saving 99
  - Social Programs 100
- Processes and Policies 100
  - Fiscal and Monetary Issues 100
  - Incomes Policies and Inflation 101
  - Saving Incentives 103
  - Labour Market Issues 104
  - Social Issues 105
  - International Trade 108
- Conclusion 110

Appendix **111**

Notes **119**

List of Tables and Charts **123**

Project Staff **127**

This report reflects the views of the Members of the Economic Council of Canada.

Members of the Economic Council of Canada

David W. Slater, Chairman
Peter M. Cornell, Director
Patrick Robert, Director

Philip C. Barter
Partner,
Price Waterhouse and Co.,
Vancouver

Pierre Brien
Vice-President,
Canada Lands Company (Mirabel) Ltd.,
Ste-Scholastique

Paul-Émilien Dalpé
Former Labour Leader,
St-Jérôme

G. Campbell Eaton
Managing Director,
Newfoundland Tractor and Equipment Co. Ltd.,
St. John's

Shirley B. Goldenberg
Professor,
Faculty of Management,
McGill University,
Montreal

T. Earle Hickey
Former Minister of Finance of P.E.I.,
Charlottetown

Kalmen Kaplansky
Senior Fellow,
Human Rights Centre,
University of Ottawa,
Ottawa

Pierre Lortie
President,
Montreal Stock Exchange,
Montreal

Donald H. McDougall
Partner,
Stewart MacKeen & Covert,
Halifax

Alastair H. Ross
President,
Allaro Resources Ltd.,
Calgary

Gerald V. Schuler
Chief Executive Officer,
Co-operative College of Canada,
Saskatoon

Patrick Shimbashi
Farmer,
Taber, Alberta

Ralph G. M. Sultan
Vice President,
Starlaw Holdings Limited,
Toronto

Douglas P. Thomas
Vice-President,
Toronto Investment Management Inc.,
Toronto

Roy Vogt
Professor,
St. Paul's College,
University of Manitoba,
Winnipeg

J. Irving Zucker
President,
Re-Vest Holdings Limited,
Hamilton

READER'S NOTE

The reader should note that various conventional symbols similar to those used by Statistics Canada have been used in the tables:

--	amount too small to be expressed
..	figures not available
...	figures not appropriate or not applicable
–	nil or zero
e	estimated figures
x	data confidential, to meet the secrecy requirements of the Statistics Act.

Details may not add up to totals because of rounding.

Preface

This year marks the Economic Council's twentieth anniversary. It seems appropriate, therefore, to re-examine briefly, in our Annual Review, Canada's economic performance over the years, to consider some of the major developments that have occurred, and to reaffirm economic objectives for the future.

When the Council was formed, the Canadian economy, then as now, was just starting to recover from an extensive period of recession. It was a time of considerable optimism. Unemployment and inflation were on their way down, and the balance-of-payments strains that had developed in the late 1950s were easing. This optimism, which was reflected in the Council's First Annual Review (1964), was generally justified by the economy's performance in the decade that followed. World trade and domestic investment were healthy. While not all of the Council's objectives were attained – the economy's average annual real growth came close to reaching the 5.5 per cent target proposed by the Council. The living standards of Canadians were rising, and programs were introduced to improve the health, income security, and educational and employment opportunities of men and women throughout the nation.

The more recent experience, however, stands in stark contrast to that of the 1960s and early 1970s. Most of the past decade has been a period of rising unemployment and inflation, slow economic growth, almost nonexistent overall productivity improvements, and increasing internal frictions over relative shares, culminating in the deepest recession in almost half a century. The deteriorating record of economic performance in the late 1970s and the severity of the recession that ensued forcefully underline the unpredictability of many of the forces that bear on our economic well-being. The titles of our recent Annual Reviews – *The Inflation Dilemma*, *Two Cheers for the Eighties*, *A Climate of Uncertainty*, and *Lean Times* – reflected the pessimism accompanying these developments. These difficulties have not been unique to Canada, however. The past decade has been a humbling period for all of the industrialized countries and for many Third World nations that were beginning to see the light at the end of the underdevelopment tunnel.

Notwithstanding these realities, we would be ill-served by gloom. The title of our Twentieth Annual Review – *On the Mend* – clearly affirms our belief that the worst is over. The underlying strength of the Canadian economy is re-emerging, and there are signs of a new vitality in a number of sectors. At the same time, there remain many areas of concern where renewed efforts must be made to reduce or eliminate the economic difficulties that still face many Canadians. This Review is devoted to an examination of those issues.

In Chapter 1 we look at some domestic developments over the past two decades that helped to shape the current economic situation. In Chapter 2 we review Canada's performance in international commerce, in light of the emergence of new markets and new twists in protectionism. In Chapter 3 we observe how Canada, along with the other major OECD countries, fared during this past recession, and we consider the prospects for recovery. We include economic projections showing that the level of real GNP will not recover to its 1981 peak until early or mid-1984 and that, over the coming years, high unemployment will remain an acute problem for Canadians.

Given the prospect of persisting unemployment and what this means in terms of output forgone, unused skills, loss of personal income, and heavy government expenditure loads for unemployment insurance and social assistance, we take stock in Chapter 4 of how severely some parts of Canada's social security system were tested during the recession and how Canada's income support system for working-age Canadians compares internationally.

Perhaps the most profound social change in Canada during the last two decades has been the increasing participation of women in the nation's wage economy. Women are diversifying their involvement and using their skills and talents in a widening variety of jobs, thereby contributing to, and strenthening, their personal and family income security. But the combination of parental responsibilities and the increasing numbers of divorces and broken marriages gives an added dimension to the employment situation of women. We consider these and related issues in Chapter 5.

Finally, it is this Council's view that Canada must build on its economic strengths, maintain the social objectives that have made it a humane and caring nation, and work towards greater prosperity through the application by all Canadians and their governments of economically efficient and prudent effort. In Chapter 6 we affirm new economic targets for the years ahead and advance a number of recommendations to help meet these goals.

On the Mend

1 From Then to Now

Over the past 20 years the composition of the labour force, the nature and location of economic activity, and the role of the public sector in Canada have all been substantially altered. In the process, major social and economic gains have been achieved; as a result, we are, on average, better educated, healthier, more prosperous, and more travelled, and we have greater access to a wider variety of public and community services than ever before. These achievements have provided a solid foundation for further social and economic development in the 1980s.

But, equally, some problems have become more acute. There have been errors of judgment, short-sighted responses to immediate pressures, and a slowness to adjust to very rapid woldwide technological advances. Canada is a country with very high unemployment; our productivity performance is among the worst of the major industrial countries; and we are still not free of cost-push inflationary pressures. Many enterprises exist only because of protective barriers; and regulations in energy, transportation, the professions, and a host of other areas distort competition and the efficient allocation of resources. Ultimately they burden Canadian consumers and reduce this country's economic potential. Virtually all governments in Canada face large budgetary deficits that limit their room for fiscal manoeuvre. These and other vexations must be balanced against the achievements, and, in the coming years, they will challenge our ingenuity.

It can be seen, therefore, that as it approaches mid-decade Canada is not without problems, particularly those associated with sustaining sufficient growth and productivity improvement to provide adequate and meaningful employment opportunities for Canadians in the years ahead. While the economy is now clearly on the mend, if the recovery is to endure, Canadians must draw lessons from the past, be realistic in their expectations, and once again assert both prudence and competitive initiative.

In Retrospect

Looking back after this recent extraordinarily difficult period, it is hard to recapture the complex conjuncture of the 1960s, characterized by partisan political bickering and occasional nationalist flag-waving, along with evident concern for greater opportunity, income security, and the elimination of poverty.

In an era when the Kennedy and Johnson Administrations were waging war on poverty in the United States, both the federal government and the provinces vied to establish programs of social opportunity in Canada. That period also coincided with new perceptions of family responsibilities, individual worth, and women's contributions outside the home. In the 1960s the U.S. Food and Drug Administration first approved the "Pill," which was to alter dramatically the patterns of demographic growth and the relationships between men and women both within and outside married life.

In Canada, the decade had commenced with a recession and with unemployment rates that had reached a postwar high. Then, as now, there were widespread worries about technological change and about the structural displacements and unemployment that it was expected to generate. There were worries, too, about Canada's lagging industrial productivity relative to that of the United States – a gap that was attributable in part to lower average schooling levels in this country. Supply-side measures were adopted to raise education and skill levels in order to confront structural unemployment and to provide a better match of manpower skills with the new job requirements. Under the federal Technical and Vocational Training Act, introduced in 1960, major funding was provided to the provinces to cover the capital costs of new facilities for secondary and technological education, as well as to retrain and upgrade the educational levels of young people and adults. Other measures were designed to ease the plight of the rural poor – most notably the Agricultural Rehabilitation and Development Act, which was aimed at facilitating the acquisition of rural and agricultural skills and at effecting the land rehabilitation necessary for a modern economy.

Most of the concern about improved social opportunity and security centred on areas and activities that, under the British North America Act, were primarily within provincial jurisdiction. Thus much of the decade was spent in discussions between the federal and provincial governments on how to achieve higher standards of, and greater access to, educational opportunities, health care, social assistance, and old age security, as all provincial governments sought to play a more active role in achieving the social and economic aspirations of their residents, in keeping with their powers under the BNA Act. And all of the provinces pressed for a larger share of personal income tax and for more flexibility in shared-cost programs.

These matters were foremost at the federal-provincial conference held in early 1964 to discuss, among other things, an improved pension system for all Canadians. The result was the implementation of the Canada and Quebec Pension Plans (CPP and QPP), with entitlements fully transferable and portable to all contributing Canadian workers. Largely at Quebec's insistence, the CPP and QPP were partially funded, with the funds being made available for borrowing by individual provinces. The consequences for Canadians were enormous: a composite old-age-protection package developed, combining universality through the basic Old Age Security (OAS) entitlement, selectivity through a means-tested Guaranteed Income Supplement (GIS), and a fully portable, earnings-related contributory pension. This package, together with private pension coverage and registered retirement savings plans, makes Canada's system of income care for the elderly more flexible than that of most other member countries of the Organisation for Economic Co-operation and Development (OECD).

There were worries, too, about the adequacy and accessibility of health care in many parts of Canada. Saskatchewan had pioneered provincial hospital insurance immediately following the Second World War; by the time the National Hospital Insurance Program was introduced in 1958, five provinces already had similar programs that were eligible for federal funding under cost-sharing arrangements. By 1961 all Canadians had become entitled to the same basic hospital-care benefits. But even then, despite the various schemes administered by either individual physicians or private insurance firms, half of the Canadian population was without medical insurance. The implementation of medicare in Saskatchewan in 1962, despite fierce opposition by the Canadian and U.S. medical associations and a fractious doctors' strike, was a first for any government in North America. In 1965 the federal government committed itself to contributing funds to provincial medicare schemes that were "universal and portable," covering all general and specialist services, and that were administered by the provinces. Despite variations in the existing private and public schemes within the provinces, by 1971 all of the latter had agreed to the program, and nationwide medicare began.

There was a widespread consensus that, wherever they live, Canadians should generally enjoy the same standards of income and health protection and have access to the same educational and job opportunities. Whatever the delivery system, be it federal or provincial, the application of generally acceptable basic standards was in keeping with the Canadian spirit of sharing between the "have" and "have-not" provinces, and it was a means of drawing together the different provinces and regions into a coherent unity. This generally accepted goal acknowledged the constitutional responsibility of the provinces in administering many of the programs; at the same time, it sought to bolster their ability to provide improved standards of access.

That was the objective that underlay the introduction of the Canada Assistance Plan, whereby the federal government shared equally with the provinces in the financing of social assistance on a needs-tested basis, with common minimum standards in all provinces. The same general goal also prompted a massive shared-cost program with the provinces in the area of postsecondary education with respect to the operating expenditures of the community colleges and universities that were required to provide the education and skill needs of the generation born during the postwar "baby boom." Under the Adult Occupational Training Program, which had replaced the Technical and Vocational Training Act, the federal government went a step further, buying designated training from the provinces for those unemployed persons who had dropped out or had long since left school, and paying them individual allowances.

The tradition of sharing was also embodied in the principle of fiscal equalization, designed explicitly to "raise the fiscal capacity of have-not provinces." By 1964 the basis of equalization was the per capita tax yield in Canada's two wealthiest provinces, taking account of natural resource revenues, and the federal government's stated objective that the equalization payments should "enable each province to provide an adequate level of public services without resort to rates of taxation substantially higher than those of other provinces." Thus through a combination of federal, provincial, and shared initiatives – sometimes with one level of government, and sometimes the other, taking the lead – the 1960s and early 1970s saw the establishment of the mix of health, educational, and social security programs that now underpin this nation's economic and social well-being. It is this enduring achievement, accomplished by many governments acting together, that stands out above all else as being expressive of the best in Canadians during that period.

This achievement did not, of course, occur without major transformations in the role of government nor without increases in the taxes paid by Canadians. By the mid-1970s the expenditures of all levels of government exceeded 40 per cent of GNE, compared with 25 per cent a generation before. Prominent was the growth in provincial spending. Whereas transfers to the provinces accounted for less than 10 per cent of the federal budget in 1955, they commanded 22 per cent two decades later. Over the same period, federal expenditures as a proportion of GNE grew from 17 to over 21 per cent (a relative increase of 27 per cent), but those of the provinces (including local governments) rose by a whopping 128 per cent – from 12 to almost 28 per cent of GNE.

Massive institutional changes of this magnitude are most easily implemented when the economy is prosperous and growing. This was the case for Canada, with annual real growth rates averaging over 5 per cent. Throughout the 1955-75 period Canada enjoyed rising exports and strong net investment. The terms of trade favoured primary exports, and there was strong mining activity throughout most of the northern parts of the provinces and in the Yukon and Northwest Territories. Grain sales to Eastern Europe were booming. In 1965 the Canada-U.S. Automotive Agreement was concluded, whereby the Canadian subsidiaries of the major U.S. automotive companies could, under certain conditions, import cars and auto parts duty-free from the United States; in addition, the United States completely eliminated tariffs on Canadian-made cars and parts. This immediately led to the rearrangement of automobile production on a North American basis, with increased specialization. In Canada, automobile production and employment rose, and by the early 1970s automobiles and parts had become the single largest export category.

Across the country, provincial governments were encouraging major domestic investment in such projects as new hydroelectric capacity development on the Columbia and Peace Rivers in British Columbia, the Nelson River in Manitoba, Churchill Falls in Newfoundland, and Mactaquac in New Brunswick. Toronto and Montreal were digging subways and building overhead skyways; and Montreal played host to Expo 67, the first international exhibition held in Canada. The urban framework was expanding rapidly to accommodate a growing population and the children of the baby boom; schools, universities, shopping centres, and assembly plants were springing up rapidly.

Increasingly, too, Canada was looking outward. In the 1960s further international discussions took place between participants in the General Agreement on Tariffs and Trade (GATT), aimed at achieving multilateral, across-the-board tariff reductions. When these negotiations concluded in May 1967, GATT members had made tariff cuts mostly on a symmetrical basis; these included major U.S. reductions that favoured Canadian manufactured and semimanufactured exports. Canada's effective rate of tariff protection dropped from 22 to 15 per cent; and, as the economy opened up further, it became more closely integrated within the fabric of North America.

With rising prosperity and the associated shift to service activities, more and more women were able to find permanent and part-time jobs in the workforce, and more young people, too, were able to find part-time employment; all of this contributed to an increase in family incomes. Organized labour was also active. Traditionally, union strength had been concentrated in the primary and secondary manufacturing industries; but, with the expansion of the service sector, an increasing organizational effort was directed there. Much of this activity took place in the public sector; by the end of the 1960s and early 1970s teachers, nurses, nonmedical hospital workers, and most public servants had secured the right to collective bargaining. In the federal government and in some of the provinces, this included the right to strike; in other provinces, grievances and disputes not resolved through conciliation were subject to binding arbitration. These developments were to have a significant impact in subsequent years.

Throughout the 1960s there had been a tendency for price increases to creep up. Very early in the decade, Canada's inflation rate was less than 2 per cent, but it had risen to close to 5 per cent by the late 1960s. Despite a modest improvement in 1970 and 1971, the spectre of inflation was looming larger. From our present juncture, it is difficult to pinpoint precisely why price increases and expectations tended to take off in 1972, but a number of contributing factors are clearly discernible. A few years earlier, the United States had broken the link between private and official gold standard prices, thereby putting the world monetary system generally on a dollar standard. This was followed by a realignment of the dollar, the cessation of its convertibility into gold, and a period of considerable exchange-rate variations. At the same time, overall demand was strong during the 1971-73 period, and most economies were operating at close to capacity. First, the prices of agricultural products began to rise rapidly, followed by those of other commodities. Then, real oil prices underwent a fourfold increase under the impetus of the Organization of Petroleum Exporting Countries (OPEC). Those years were marked by a highly accommodating monetary policy, with the money supply (broadly defined) in the major industrial countries rising at rates in excess of 20 per cent. The combination of the business surge, the rapid rise in oil and other commodity prices, and the increase in domestic money supplies and international liquidity could only lead in one direction. In 1974 and 1975, even though the cycle had peaked and GNP growth had slowed severely, consumer price indexes averaged double-digit rates in the OECD countries (including Canada), albeit with wide variation between them.

In keeping with prudent contracyclical budgeting, economic buoyancy and rising inflation should normally have resulted in large federal fiscal surpluses. But the combination of rising revenues and unemployment levels that were deemed to be far too high at the time (although they largely reflected very strong labour force growth, particularly among those members of the baby-boom generation who were then reaching employment age) prompted what seems to have been an excessively accommodating monetary stance and fiscal stimulation. Although the expansion of the unemployment insurance system in 1971 to cover almost all employed persons, with substantially increased benefits and reduced qualifying periods, eased much of the pain of unemployment, it also encouraged a further increase in labour force participation that helped to sustain the high unemployment rates. Experimental programs of temporary job creation, such as Opportunities for Youth and the Local Initiatives Program, had similar consequences. Most entitlement benefits, including unemployment insurance, manpower training, and old age security, were effectively indexed one way or another, and rising prices and wages meant heavier nominal expenditures. When it was decided in 1973 to index the personal-exemption portion of the personal income tax, most of the inflationary bias built into the revenue side was eliminated. Thus when the post-OPEC recession occurred in 1974, without any evident easing of inflationary expectations and pressures, the federal budgetary surplus quickly turned into a deficit. Most of the provinces – except Alberta, which was benefiting from the rise in oil prices – also recorded deficits. Note, however, that Canada was not alone in experiencing the relatively unfamiliar combination of economic stagnation and built-in inflation; most OECD countries were undergoing similar problems.

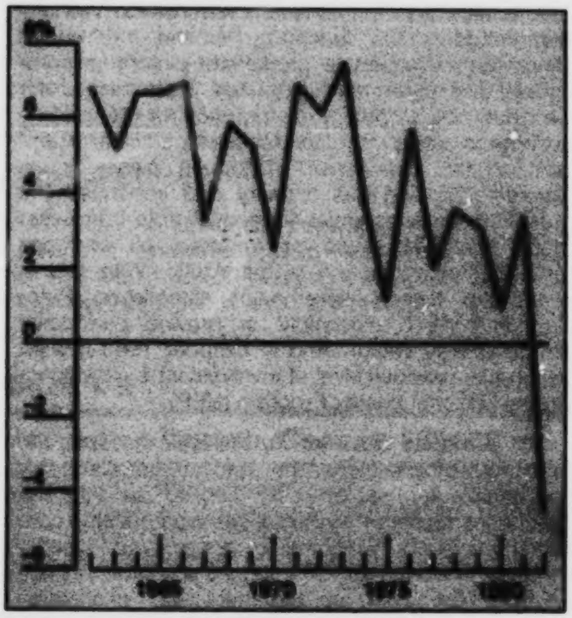
The initial rise in energy prices created many difficulties, directly and indirectly notching up the inflation rate, raising inflationary expectations, and giving rise to concerns over Canada's energy self-sufficiency. In 1973 the federal government decided to control all oil exports. As the world price increased relative to the domestic price for Alberta crude, Ottawa adopted a two-price policy, whereby Canadian oil prices were to be held at roughly 75 per cent of the world price. This meant that massive subsidies had to be paid to the Atlantic provinces and to Quebec in order to make up the difference between the prices of the oil that these provinces were importing from abroad and the price of the domestic oil purchased by the rest of the country. Much of this was paid for by taxes on oil exports, and this whole policy resulted in inevitable squabbles between Ottawa and Alberta over royalties, profits, and taxes.

By 1975 the economic situation had severely deteriorated: real growth had slumped; unemployment had increased; the balance-of-payments deficit had widened; and, despite next-to-zero productivity gains, a growing number of negotiated annual wage increases in both the public and private sectors reached 20 per cent or higher. In the fall of that year, the federal government introduced its anti-inflation program. Developed with the acquiescence of provincial governments, which in turn took pains to regulate rental increases, the anti-inflation program established a board to monitor price increases and to contain wages on the basis of a formula that called for increments, over a three-year period, of roughly 8, 6, and 4 percentage points above the allowance for productivity gains. Limits were also placed on markup ratios; for the most part, however, these were without effect. These measures were coupled with plans by the Bank of Canada to reduce the rate of monetary expansion. While the program was widely accepted at the time and was generally considered to have been an important factor in curbing wage expectations, it contributed to escalating tensions between organized labour and the federal government. Within a year, however, inflation rates dropped substantially, although clearly this did not reflect a fundamental or long-term solution to the "stagflation" phenomenon.

Notwithstanding that immediate improvement, Canada's subsequent economic performance was weak, in part because of the uncertainties engendered by persistent inflationary expectations, the overvaluation of the Canadian dollar (which was trading at over $1 U.S.), and poor productivity performance. While reduced economic performance in the second half of the 1970s was characteristic of the other major OECD countries as well, Canada's experience on most fronts was particularly discouraging.[1]

Chart 1-1

Annual Growth Rate of Real GNE, Canada, 1962-82

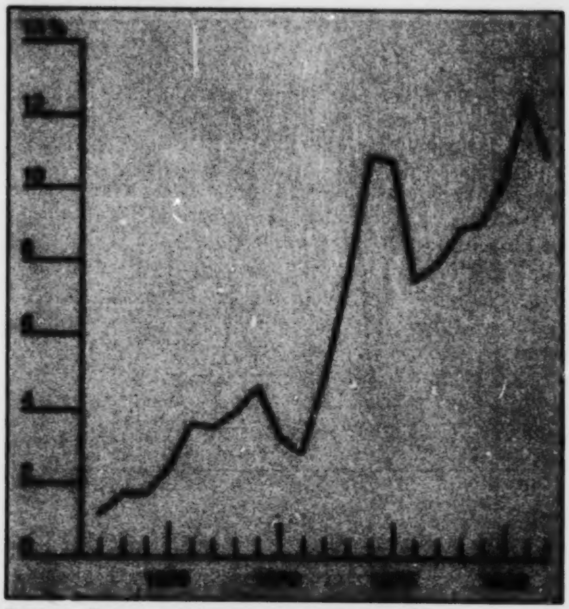


SOURCE Based on data from Statistics Canada.

The extent of the steady deterioration in economic performance is clearly apparent from the picture provided by Charts 1-1 to 1-4. Annual growth, despite year-to-year variations, trended down from the early 1970s, as did the annual growth rate of productivity in commercial industries. Inflation rates soared, and by 1980 they were back at double-digit levels, despite the dampening effect brought about earlier by the Anti-Inflation Board and despite the efforts by monetary authorities to keep the growth of the money supply within fairly narrow bounds. And the trend rate of unemployment, after pausing at around the 8 per cent level for several years, climbed steadily as the recession deepened. We shall return to these economic comparisons in Chapter 3.

Chart 1-2

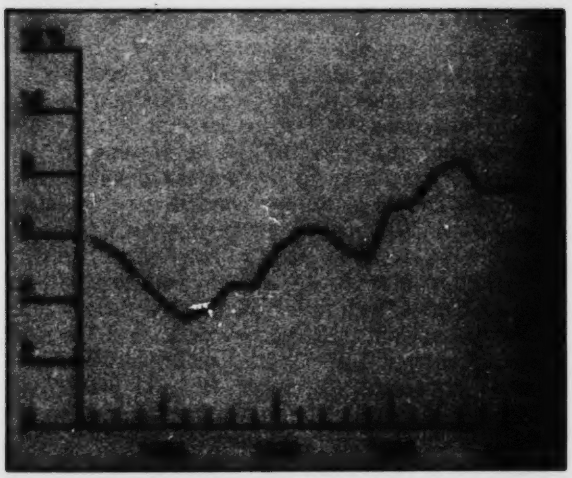
Annual Growth Rate of the Consumer Price Index, Canada, 1962-82



SOURCE Based on data from Statistics Canada.

Chart 1-3

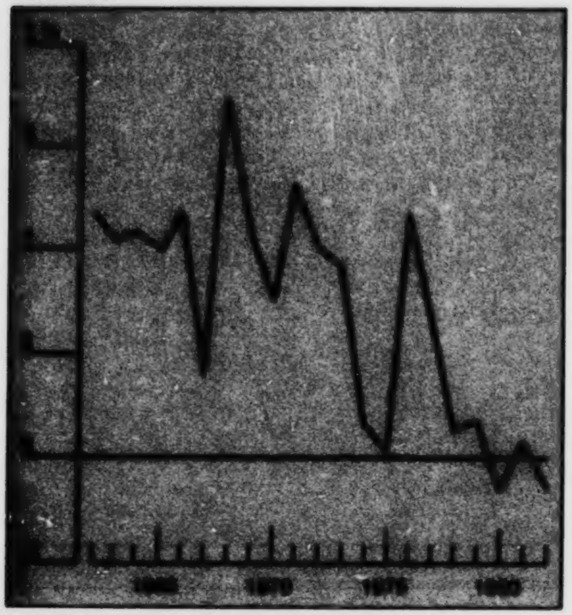
The Unemployment Rate, Canada, 1962-82



SOURCE Based on data from Statistics Canada.

Chart 1-4

Annual Growth Rate of Productivity[1] in Commercial Industries, Canada, 1962-82



[1] Defined here as output per person-hour.
Source Based on data from Statistics Canada.

During this period, expenditures at the federal and provincial levels continued to mount more rapidly than revenues, except in Saskatchewan, Alberta, and British Columbia. In order to curtail rising costs and to meet provincial demands for greater program flexibility and accountability, the federal and provincial governments agreed in 1977 to end some of the shared-cost programs, to transfer tax points to the provinces, and to ease the conditionality of other federal-provincial transfers. Although federal expenditures on goods and services trailed GNP growth throughout most of the period from the late 1970s to the early 1980s, with rising inflation the government had to keep increasing the yields on new Canada Savings Bonds and to give bonuses on old issues in order to encourage the public to keep them. The government's fiscal stance was further aggravated by the combination of new increases in world oil prices, which raised the cost of the oil import subsidies, debt-service payments, and transfers of income to businesses or individuals for a variety of purposes, the most important of them being to combat unemployment.

While Canadians have traditionally depended on foreign savings for domestic public and private capital investment, some have long worried about the extent of foreign ownership in various sectors of the Canadian economy. These concerns, together with several important takeover initiatives by foreign corporations, prompted the government in 1973 to introduce the Foreign Investment Review Agency to screen foreign investments entering Canada and to ensure that "Canadian interests were well served" by them. Indeed, the federal goverment had earlier shown an inclination to participate directly in commercial investment activities, when it established the Canadian Development Corporation in 1971. The upsurge in world oil prices focused particular attention on the dominance of foreign ownership in Canada's oil and gas industry and enhanced the prospects for substantial economic rents from what many predicted would be immense oil and gas recoveries offshore and in the Arctic. With this in mind, the federal government established Petro Canada in 1975, ostensibly to "provide a window" on the energy sector. And in October 1980 it went beyond its previous level of involvement by announcing the National Energy Program (NEP).

Still in a state of evolution, the NEP reasserts the objectives of energy security and greater Canadian ownership. Another objective has to do with the sharing of resource rents between producers, consumers, and the two levels of government. Clearly, however, the original NEP imposed a regime of price controls, new taxes, and regulations that challenged the earnings positions of both the oil-producing companies and the provinces. The exodus of investment capital that followed contributed to the country's difficulties. Subsequent negotiations, principally with Alberta, reduced the unilateral nature of the NEP and led to a federal-provincial accord on oil and natural gas pricing, taxation, and exploration incentives. However, the unanticipated reduction in the world oil price and the current drop in the U.S. market for Canadian natural gas exports have complicated the issue. New arrangements worked out in the summer of 1983 will last only until the end of 1984. (Space precludes our doing justice here to the extreme importance of energy developments for Canada in both the past and the future. We have, however, devoted very considerable study to this issue and will publish a full report on energy in 1984.)

Clearly, over the past decade Canada's poor economic performance, the very size of the entitlement programs on which this nation's health, education, and social security systems are built, along with the growth in provincial expenditure commitments that these programs entail and with the indexation of the personal income tax and many other changes, have deeply affected the federal government's financial ability to manage the economy. The built-in stabilization features of the fiscal system have increased, leaving less room for discretionary contracyclical stabilization policy. Collectively, the role of the provinces in economic matters has become far more important than it was several decades ago. As a result, more than ever before both levels of government, within their constitutional powers, need to work together in ways that are consistent with the common concern for renewed economic vitality. The extent and frequency of federal-provincial and first ministers' meetings attest to the need for this process on many practical issues.

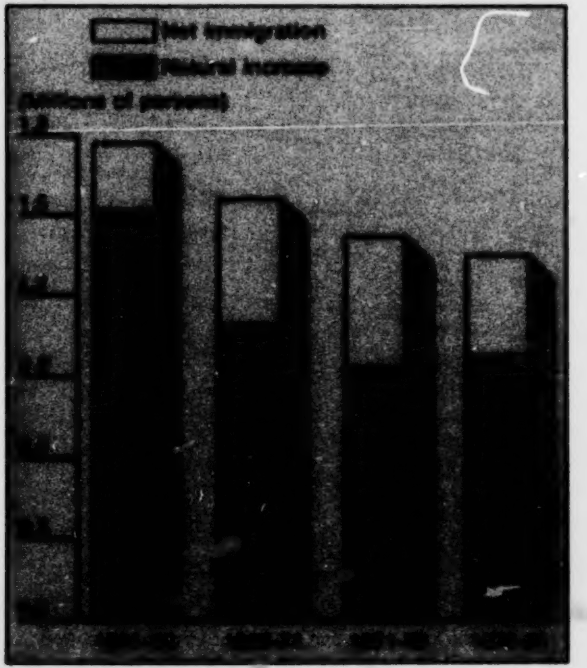
Taking Stock

Today, the Canadian population is older, more urbanized, more educated, and more ethnically diverse than it was 20 years ago. More Canadians are working, and more are unemployed. Population growth has slowed steadily – from almost 2 per cent annually in the early 1960s to just over 1 per cent in the late 1970s – and it will likely decline further over the rest of the 1980s (Chart 1-5). Many women are postponing having children until their late 20s or early 30s, and few are bearing children after age 35.

As a consequence, immigration will likely continue to form a vital component of population growth, thereby contributing to this country's cultural enrichment and ethnic mosaic. Canada has benefited greatly from immigrants; they have contributed to the nation's productive effort through their know-how and skills, and they have strengthened and diversified consumer demand and contributed to economic growth. Nearly one in every six Canadians was born outside this country. And while inflows from Europe – traditionally the main source of immigration – have diminished, the number of Canadian residents born in Asia, the West Indies, and Central and South America has increased very substantially. We believe that this country derives strength from its ethnic diversity and from its role in meeting worldwide

Chart 1-5

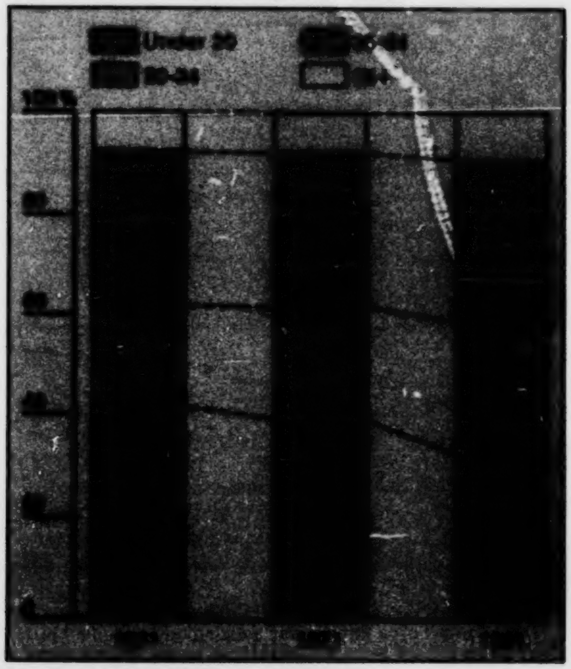
Population Growth, Canada, 1961-81



Source Based on data from Statistics Canada.

Chart 1-6

Age Distribution of the Population, Canada, 1961, 1971, and 1981



Source Statistics Canada (CANSIM).

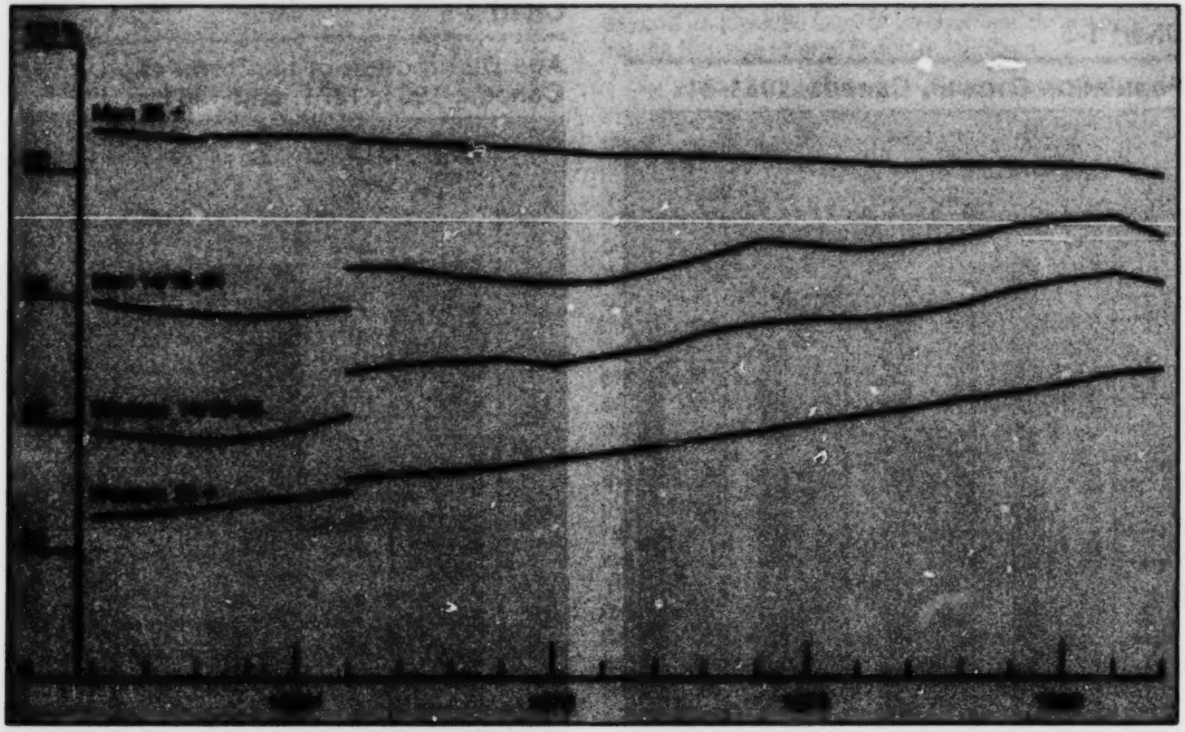
humanitarian concerns – through the resettlement of refugees from various continents, for example.

Canadians have aged. A generation ago, the median age of the postwar "baby boomers" was about 10 years; now, it is about 30. And while the ranks of the elderly (i.e., those aged 65 and over) have grown, the major expansion in their numbers is still a few decades away. In one sense, therefore, Canadians are currently in a very advantageous position. The swift decline in the proportion of the young and the modest growth in the proportion of the elderly have meant that the size of Canada's working-age population, relative to that of its dependent population, has grown significantly (Chart 1-6). This shift has also contributed to an increase in the aggregate saving rate.

Interlinked with this demographic development are profound changes in the structure of Canada's labour force, most prominently the rise in the participation rates of women and young people (Chart 1-7), as well as the decline in those of men over 55, which reflects a trend towards earlier retirement. Two decades ago, men and women aged 25 and over accounted for 60 and 18 per cent of the labour force, respectively, while those between the ages of 15 and 24 represented 22 per cent of the total (Table 1-1). Today, the relative importance of adult men has dropped to about 46 per cent; the proportion of women – with the decline in birth rates and the increased labour force participation of mothers with young and school-age children – has increased to close to 30 per cent; and young people, many in part-time or part-year jobs, account for 25 per cent.

Chart 1-7

Labour Force Participation Rates, by Sex and Age Group, Canada, 1961-82[1]



---

[1] The Labour Force Survey was substantially modified in 1975. In particular, the lower age limit for labour force participation was raised from 14 to 15. Statistics Canada revised some data series back to 1966 in line with the new definitions. This explains the break in the data between 1965 and 1966.

Source Statistics Canada (CANSIM).

Table 1-1

Composition of the Labour Force, by Sex and by Age Group, Canada, 1962, 1972, and 1982

	1962[1]	1972	1982
	(Per cent)		
Men			
15-24	13.1	14.5	13.4
25-54	48.3	41.2	38.0
55 and over	11.4	9.5	7.5
Subtotal	72.8	65.2	58.9
Women			
15-24	8.8	11.6	11.6
25-54	15.5	19.5	25.8
55 and over	2.9	3.7	3.7
Subtotal	27.2	34.8	41.1
Total	100.0	100.0	100.0

1 Based on the old Labour Force Survey, which included 14-year-olds.
SOURCE Based on data from Statistics Canada.

Almost 60 per cent of Canadians live in cities with a population of more than 30,000 – 45 per cent in the ten largest metropolitan areas from the Atlantic to the Pacific. At the same time, nearly 70 per cent of working Canadians are now employed in service-related activities; less than 7 per cent work directly in agriculture and other primary industries, which have traditionally been the nub of Canada's comparative advantage in international trade. Yet, despite urbanization, the rural and resource roots of Canada's economy persist, although in much less isolated form than heretofore. The farm consolidation and off-farm movement that were still under way in the 1960s have generally been arrested, thanks to the relative improvements in farm productivity and in food prices, and the number of persons in agriculture has now more or less stabilized at just under 5 per cent of total employment. Not all, of course, are in full-time farming; indeed, a large majority of them report higher earnings from nonfarming activities. However, those who are fully engaged in farming appeared, at least before the recession, to be earning returns that were comparable to those of other self-employed businesses.[2] Mining, forestry, and energy extraction continue to be vital components of the economy; and while they are highly capital-intensive industries, their prosperity imparts a high employment leverage to other sectors of the economy. As a result, and indeed as the nation's productive capabilities have become more diversified and as small manufacturing and other business enterprises have taken on more importance, there has been a resurgence of smaller cities and medium-sized towns. During the 1970s these centres grew more rapidly than the larger cities for the first time since the Second World War.

During two decades of growth and altering industrial structure, and despite substantial geographic movement of individuals and families, the character and flavour of Canada's diverse regions have changed only slightly. The main effect of the net migratory trends has been to increase the populations of Alberta and British Columbia. The net exodus from Quebec has been continuous, while Ontario has shifted from being a province of heavy in-migration to one of net out-migration; as for the Atlantic region, after years of out-migration, it is now experiencing net inflows (Table 1-2). More recently, the extraordinary flow of migrants to Alberta in response to burgeoning oil and gas developments has shown clear signs of abating.

Table 1-2

Net Interprovincial Migration,[1] by Province, Canada, 1961-80

	1961-65	1966-70	1971-75	1976-80
	(Thousands of persons)			
Newfoundland	-12.6	-19.8	4.1	-6.8
Prince Edward Island	-2.1	-3.1	2.7	1.7
Nova Scotia	-21.5	-16.5	10.6	1.3
New Brunswick	-20.7	-21.5	17.2	6.2
Quebec	-19.1	-116.3	-81.8	-154.8
Ontario	70.2	152.1	-23.5	-53.6
Manitoba	-24.0	-50.5	-30.4	-49.1
Saskatchewan	-37.2	-78.9	-37.9	10.4
Alberta	-2.6	25.1	49.8	146.3
British Columbia	69.6	129.4	89.2	98.4

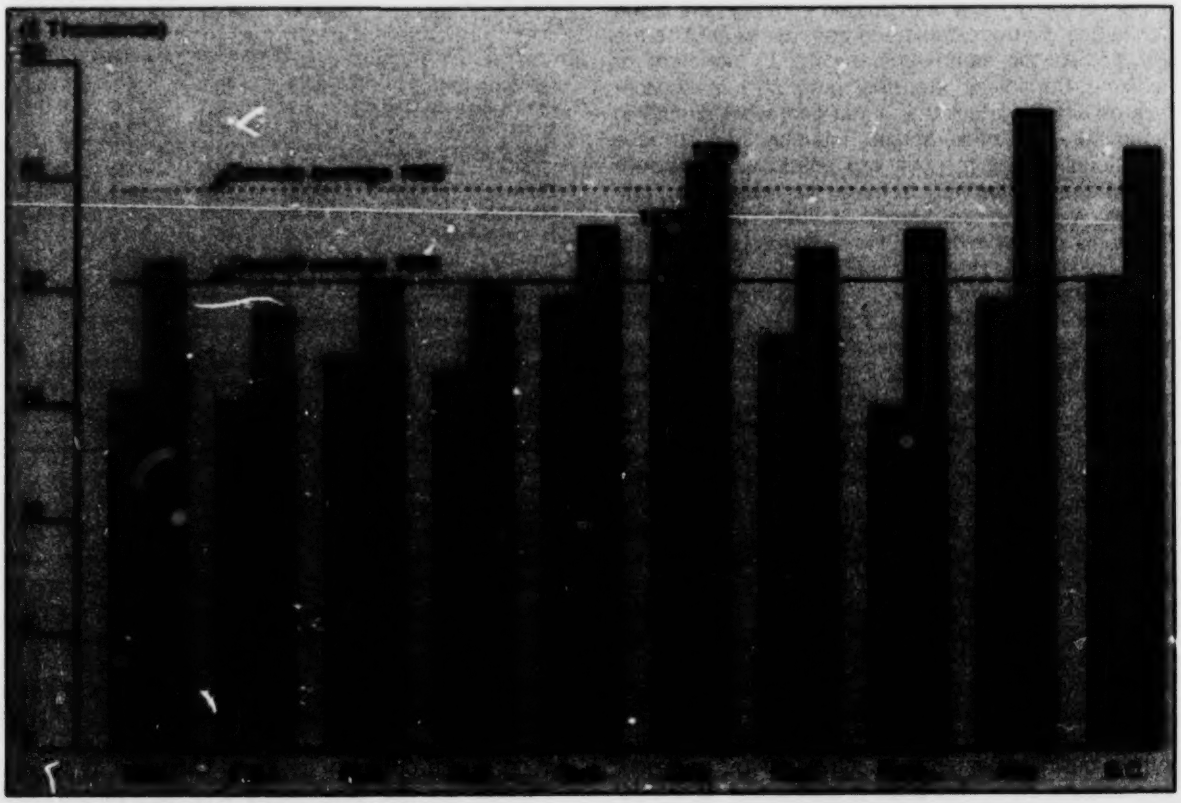
1 Excluding moves to or from the Yukon and the Northwest Territories.
SOURCE S. Winer and D. Gauthier, *Internal Migration and Fiscal Structure: An Econometric Study of the Determinants of Interprovincial Migration in Canada*, Economic Council of Canada (Ottawa: Supply and Services Canada, 1982).

Canadians today are, by any standard, well educated and skilled. Thanks to the emphasis and resources given to education and training, access to learning has expanded, and the range of courses, programs, and instructional institutions has grown. This Council has always considered investment in education as crucial to the nation's economic performance and as a means of providing individuals with greater economic opportunity. And while some of our earlier optimism has been tempered by market realities, we are encouraged by the changes that have taken place in enrolment patterns. The main thrust occurred during the 1960s, when enrolment rates in postsecondary institutions and community colleges almost doubled.[3] Although the progressive aging of the baby-boom generation has since resulted in a diminution, first, in the number of elementary and secondary students, and then in full-time university undergraduate enrolment from 1977 to 1981, many more working Canadians are now studying. Indeed, more than a quarter of a million people register as part-time students in credit courses at Canadian universities, and part-time students now account for almost 40 per cent of total undergraduate enrolment. Improvements in education have taken place at every level of schooling; as a result, Canada has effectively closed the two-year gap with the United States that existed in average years of schooling. The relative number of young Canadians completing high school has risen: whereas there were 47 high school graduates for every hundred 18-year-olds in 1969, that ratio had risen to 62 in 1979. In addition, there has been massive diversification in nonuniversity institutions. Full-time enrolment at community colleges alone is now two-thirds that of universities.

Canadians enjoy substantially higher real incomes today than they did a generation ago. This is largely due to the economic vigour of the 1960s and early 1970s and to the increasing labour market participation by women and young people, which has contributed to the growth of real family incomes. On average, the latter rose annually by 4 per cent over the 1965-75 period (roughly 47 per cent over the decade), compared with just over 1 per cent from 1975 to 1981 (with indications that it fell in 1982). Viewed in a regional perspective, individual and family incomes in the Atlantic provinces still trail the

Chart 1-8

Average Household Income in Constant (1980) Dollars, Canada, by Province, 1970 and 1980



Source Based on data from Statistics Canada.

Canadian average, but the gap has narrowed. Over the most recent census decade, families in Saskatchewan, Alberta, and Newfoundland enjoyed the largest gains, while those in Ontario and Quebec recorded the smallest increases (Chart 1-8). Lying behind these averages, of course, is a diversity of situations, reflecting in part the greater generosity of the transfer programs described earlier.

The Economic Council has, since its inception in 1963, been concerned with questions of income distribution, and in its First Annual Review it set the equitable distribution of rising incomes as one of the basic economic and social goals of Canadian society. Since about 1965, however, employment opportunity, social policy, and demographics have contributed to some greater inequality in incomes between individuals and families, even though there has been a narrowing between regions. This has been due partly to the tilt towards old and young households, which traditionally manifest large income differences, and partly to the widening gap between the earnings of single- and multiple-earner families.

Families where the wife works outside the home – a type that is becoming more and more common – have recorded the highest average income levels and growth rates in relation to all types of families and individuals. On the other hand, a much more difficult situation prevails in single-parent families headed by mothers, which now represent one of every six families with children. Many are caught in the so-called "welfare trap": even if they can find suitable employment, the wage incomes that they earn, more often than not, precipitate a steep reduction, if not a total cessation, of social assistance benefits. We shall return to these issues in Chapters 4 and 5.

Thus the ethnic make-up, knowledge levels, and incomes of Canadians are very different today from what they were two decades ago. But, while real incomes and living standards have advanced substantially, though more slowly in recent than in earlier years, many remain at an economic disadvantage, even with the extensive social security structure that exists. The persistence of unemployment, the threat of renewed inflationary pressures, and the fiscal complexities of governing remain deeply worrisome.

Bearing the Costs

Table 1-3 provides a glimpse into the amplitude of Canada's social security system, in terms of government expenditure. Along with the unemployed, the elderly and the retired, the system provides special support to veterans, native groups, injured workers, the disabled, and those otherwise in severe economic distress. Old-age security benefits are the largest single component; and, with the progressive aging of the population, the number of pension recipients has more than doubled over the last two decades. Almost 60 per cent of the social security expenditures in fiscal year 1981/82 were accounted for by three items – OAS and GIS benefits, unemployment insurance, and the Canada Assistance Plan. Since then, unemployment insurance expenditures have soared.

Table 1-3

Social Assistance Expenditures by Governments, Canada, 1962, 1972, and 1982[1]

	1962	1972	1982
		($ Millions)	
Family and youth allowances	520.8	637.1	2,019.5
Federal tax credits to families	-	-	1,101.2
Provincial tax credits and rebates	-	-	1,302.5
Veterans' allowances and pensions	253.2	308.6	912.5
Unemployment insurance	409.2	1,814.7	5,398.7
Workers' compensation	93.2	239.4	1,311.3
Canada manpower training	-	169.3	199.4
Old-age security[2]	625.1	2,205.3	8,585.3
Canada and Quebec Pension Plans	-	192.7	3,314.9
Old-age assistance	61.6	-	-
Allowances to the blind and to the disabled	38.4	11.3	-
Unemployment assistance	175.8	2.1	-
Mothers' allowances	48.1	-	-
Canada Assistance Plan	-	1,431.0	5,094.0
Federal social assistance and services to Indians	-	53.2	219.0
Vocational rehabilitation for disabled persons	-	13.0	78.6
Other provincial welfare programs	115.9	297.6	2,538.3
Municipal welfare programs	42.6	132.8	437.1
Total	2,383.9	7,478.2	32,512.5

[1] Fiscal years ending March 31.

[2] Includes the OAS pension, the Guaranteed Income Supplement, and the spouse's allowance.

SOURCE Health and Welfare Canada, "Social Security Statistics, Canada and the Provinces, 1953/54-1981/82," Information Systems Directorate, Ottawa, 1983.

The upshot has been strong growth in transfers to persons and marked growth in the importance of transfer payments relative to other sources of personal income (Table 1-4). As well, the growth in the role of government as a provider of goods and services has led to a major increase in the relative importance of government wages and salaries.

Combining these two elements yields a rough indication of the share of personal income that originates directly from government. While this has leveled off since 1977, partly in response to the federal government's explicit attempt to align the growth in its spending with the trend growth of GNP, it is apparent that many Canadians are now much more heavily dependent on government payments for their economic well-being and, consequently, that they and other Canadians are taxed much more heavily than they were a generation ago.

Table 1-4

Government and the Distribution of Income, Canada, 1961-81

	Transfers to persons as a proportion of personal income	Government wages as a proportion of total wages	Share of personal income originating directly from government
		(Per cent)	
1961	9.0	19.4	22.5
1962	8.9	19.6	22.3
1963	8.6	19.8	22.2
1964	8.5	19.9	22.4
1965	8.3	19.7	22.2
1966	8.1	20.1	22.3
1967	9.2	21.1	24.3
1968	9.8	22.0	25.4
1969	10.0	22.6	26.0
1970	10.5	23.1	27.0
1971	11.1	23.7	27.9
1972	11.8	23.7	28.4
1973	11.4	23.2	27.6
1974	11.9	23.5	28.2
1975	12.5	24.4	29.5
1976	12.5	24.6	30.1
1977	13.0	24.9	30.7
1978	13.1	25.0	30.6
1979	12.5	24.2	29.5
1980	12.8	24.3	30.0
1981	12.5	24.2	29.4

SOURCE Based on data from Statistics Canada.

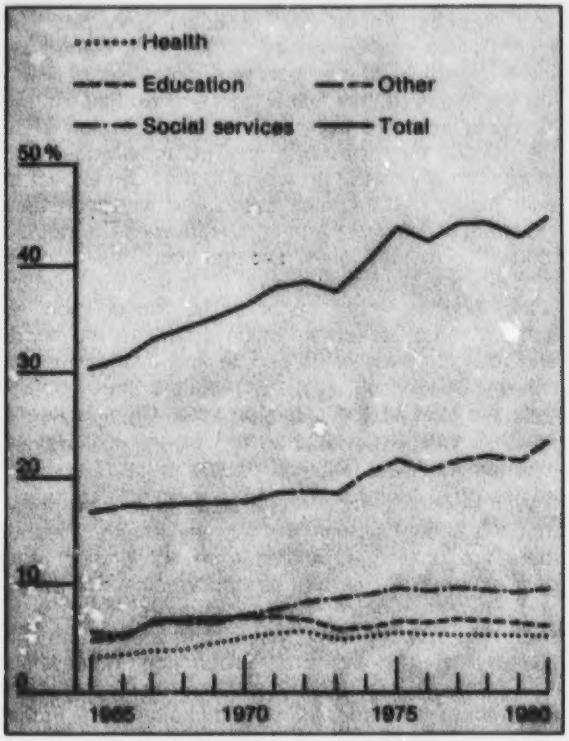
Many regard this heightened dependence on the public sector with mixed feelings. Canada has not been alone, of course, in witnessing this expanding role of governments; virtually all industrialized countries have undergone a significant enlargement of the public sector in response to social demands. Indeed, among OECD countries Canada is about mid-range in terms of the ratio of government expenditure to nominal GNP. Over the last two decades, overall government spending in Canada relative to GNP has increased less rapidly than in West Germany, Sweden, and the Netherlands but more rapidly than in the United States, France, and Japan.

The foregoing figures reflect only part of government's participation in the economy, however. They do not take into account the role of government-owned and -controlled corporations or the influence exerted by governments through the tax system and through regulations that mainly affect private, rather than government, spending. While it is difficult to assess how important these aspects of government activity are to the performance of the economy, there is clear evidence that the use of tax incentives or "tax expenditures" increased from the 1960s to the 1970s, along with a continued expansion of regulation in the Canadian economy.[4] Government-owned and -controlled corporations have also become more important in recent years; public participation in the financial and resource sectors, in particular, has grown. By 1980 federal and provincial government enterprises accounted for some 15 per cent of total corporate assets in Canada.

There can be little doubt that Canadians value, and are prepared to pay for, high standards of health, education, retraining, and income security. In the flush of the program initiatives undertaken in the 1960s and early 1970s, the share of social expenditures inevitably mounted as a percentage of GNP. In the case of health care, for example, public spending substituted in part for expenditures that would otherwise have been borne privately; as access to the programs became more universal, its proportion of GNP expanded. During the initial period of strong economic growth and rising family incomes, the sting of increased taxation was not hard to bear. With mildly accelerating inflation and the absence of indexation in the tax system, governments saw their revenues rise rapidly, making it comparatively easy for them, in the short term, to accede to demands for social expenditures to provide against various forms of deprivation. Between 1965 and 1975 total government expenditures in health, education, and welfare moved from 13 to 22 per cent of GNP (Chart 1-9). Thereafter, the climate for social spending underwent an abrupt change when the combination of sluggish growth, rising unemployment, and the effective indexation of personal income taxes and many of the entitlement programs set limits on the financial capacities of governments. Annual unemployment insurance costs increased almost fivefold from 1970 to 1975, and amendments were introduced after 1975 to contain UI benefits and to offset some negative work incentives without jeopardizing the universality and basic-income-support goals of the program. Some of the other programs, however, involved ongoing commitments that could not easily be reduced, especially where, as with the UI scheme, deteriorating economic conditions led to an increase in the number of eligible recipients.

Chart 1-9

Consolidated Government Expenditures as a Proportion of GNP, by Component, 1965-80



SOURCE Based on data from Statistics Canada.

There were some offsetting factors. First, the drop in elementary and secondary enrolment, together with a leveling-off of university enrolment, enabled governments to make some progress in reducing the share of resources committed to education. Also, once the basic health infrastructure was well in place, the provinces became relatively successful in controlling health care costs while meeting the agreed condition of universal accessibility. Indeed, as a percentage of GNP, total health care costs in Canada did not increase over the 1970s; in the United States, where private care arrangements predominate, that proportion rose considerably.[5] Canadians can feel a sense of accomplishment. Public protection in hospital care and medical services (though not pharmaceuticals) is at least as extensive as in other major OECD countries; yet total health care expenditures as a proportion of GNP increased the least in Canada over the 1971-80 period (Table A-1).

There have been counteracting pressures, however. Substantial settlements with physicians have recently increased costs in some provinces. The inclination of medical practitioners to opt out of medicare, to impose extra billing, or to urge the application of user fees in hospitals, while not adding to government health expenditures, has increased the private share of health costs and the nation's total health expenditures relative to GNP.[6] In education, a 15 per cent decline in the student/teacher ratio at the elementary and secondary levels over the course of the 1970s helped to sustain costs. Government expenditures in postsecondary education grew not only because of expanding enrolments but also because, as a matter of policy, governments assumed an increasing proportion of costs. It is significant, for instance, that fees, which accounted for about 18 per cent of postsecondary education spending in 1961, covered less than 9 per cent of spending in 1980.

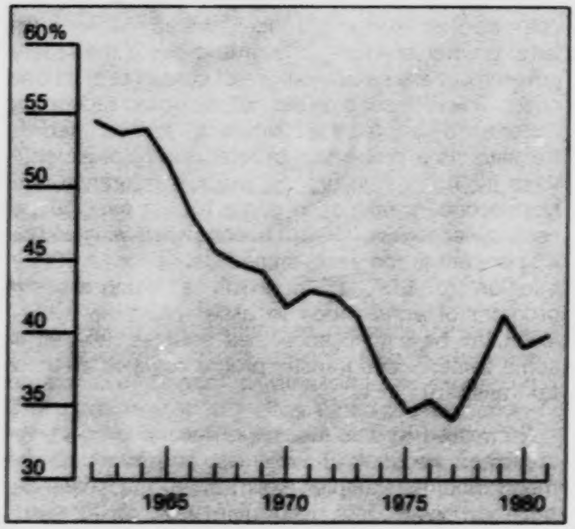
Since many health, education, and social security initiatives fall under provincial jurisdiction, it is not surprising that provincial expenditures as a share of GNP have more than doubled since 1961. Traditionally, of course, much of this effort has been funded under shared-cost arrangements with the federal government. The 1977 Established Programs Financing (EPF) arrangements resulted in federal support taking the form of per capita cash transfers and tax-point transfers to the provinces, thereby allowing the latter greater spending choice and giving the federal government a greater measure of control over its own costs. The EPF accords did not, however, reduce the importance of federal transfers; indeed, federal transfers as a proportion of total provincial expenditures for hospital insurance, medical insurance, and postsecondary education came to just over 46 per cent in fiscal year 1980/81, compared with around 43 per cent in the years immediately prior to EPF. In addition to EPF, there exists a comprehensive program of equalization to assist provinces with a lower tax base to finance their services, as well as some small federal transfer programs (such as those for transport).

Buttressed by this cushion of federal support, the combined account of provincial and local governments and the hospital sector over the years has been in only modest deficit relative to GNP.[7] Since the provinces are more dependent than the federal government on indirect taxes, which are less elastic than income taxes, they did not enjoy the same revenue growth as the federal government during the early period of economic robustness nor did they suffer from the subsequent revenue shortcomings. Indeed, the aggregate provincial balance improved overall during the latter part of the 1970s, mainly because of rising energy revenues, but it moved back into the red in 1982. The CPP/QPP account has generated a surplus every year, although this has been diminishing slowly over time.

The effect of all these arrangements has been to place the primary task of financing Canada's comprehensive system of social services on both levels of government. Some would relate these developments to the growth of the federal deficit. As a percentage of GNP, however, federal spending (including transfers to other governments) did not increase from 1975 to 1980, and it increased thereafter because the denominator (real GNP) declined during the recession. Rather, the growing deficit was due to a downturn in revenues relative to GNP, owing to the relatively weak economic conditions of the late 1970s and early 1980s, which had not been anticipated when personal income tax indexation was introduced in 1975. While the size of the federal deficit today is indeed worrisome, both in nominal terms and relative to GNP, the federal government's debt/income ratio is still below the levels recorded in the mid-1960s (Chart 1-10).

Chart 1-10

Gross Debt of the Federal Government as a Proportion of GNP, Canada, 1962-81



SOURCE *Public Accounts of Canada.*

From Now Till Then

It is clear that the kinds of safety nets that were put in place in the 1960s (and, in some cases, subsequently modified) have taken on greater importance as unemployment has been stretched to the bounds of social endurance and as the population has aged and requires greater use of health services. The recent years of slow growth have made Canadians more conscious of the costs and difficulties of meeting the needs of their fellow men and women. As the economy emerges from its deepest recession since the 1930s, they can look forward to stronger and more normal years of growth, and they can expect to earn higher real incomes associated with increased industrial productivity and competitiveness, *if they so resolve*. Provided that Canada can sustain the recovery and economic growth while keeping inflation within bounds, there ought to be ample room to achieve those objectives which attend to the social and related needs of its people and to improve the delivery of services. In many respects, these objectives are part of the same process. Canada needs healthy, educated, skilled, and secure citizens to keep the economy competitive, and vice versa.

With economic recovery in sight, it is appropriate that we should assess the journey ahead. Clearly, there are challenges arising from our present and past experiences, as well as opportunities for public and private initiative. More and more, Canada is becoming part of a world that is both specializing and diversifying, with industrial production increasingly aimed at world markets and with enormous prospects for international trade, travel, and capital flows. In this global environment, Canadian producers must assert their competitiveness by exploiting those endowments – skills, ingenuity, and natural resources – in which they have a comparative advantage. To remain competitive, Canadians must continually adapt to change, be prepared to abandon enterprises and industries that are no longer commercially viable, and encourage the movement of labour and investment capital to more favourable and profitable activities. This is best facilitated in an economy that is growing and open, and in which the individual costs of adjustment are cushioned by programs that bridge the transition without impeding or aborting it. There will always be tension between individuals and groups that seek protection and those which engage in vigorous competitive activity, not only with respect to international trade and investment but also within the domestic economy. A major task ahead for governments will be to resist the demands of interest groups who seek to eliminate competition through regulated markets or who pressure governments in ways that unduly add to costs and contribute to inflation.

A further urgent task will be to bring down unemployment and reconcile the displacement of workers with the employment opportunities that technological change will inevitably bring. It is not at all clear what the introduction of robotics, microchips, and other developments in the informational and biogenetic fields will mean in terms of jobs and skill requirements. Many jobs will be replaced by those requiring skills attuned to electronic instruments or cybernetic production processes. Conceivably, the lines between full-time, part-time, and part-year jobs will become more blurred, as will the distinction between blue- and white-collar activities. Whatever the result, the educational and working roles of men and women will continue to evolve, hopefully in the direction of greater equality of opportunity. Whether the social trend to smaller families and less-enduring marriages will continue is open to speculation, but clearly the disruptive impact of social change will be easier to accommodate if the economy is prosperous and if adequate community amenities are available.

The goals of economic growth and reduced unemployment will not be attained without a healthy business sector. While the recent fascination in some quarters with mega-projects as engines of growth has faded into more realistic expectations, it is worth recalling that the small-business sector has accounted for much of the employment growth in Canada in recent years and will likely continue to do so. Business survivors have emerged from the recession in a much leaner condition; yet some remain in a fragile state, needing to improve their balance sheets. The restoration of a climate favourable to the refinancing and birth of new business is a desirable means of promoting the growth and diversification of the economy. However important it is to address social issues, government policies must be very carefully considered so as not to impose unreasonable burdens on the corporate sector and on the individual consumers and investors who must ultimately foot the bill, as that in turn could heighten the risk of aborting the recovery.

Demographically, for the medium term, two things are evident. We are a population that is gradually aging, and the elderly will command an increasing share of resources in the years to come. And, given the decline in birth rates, immigration will remain important and will continue to contribute to the ethnic diversification of the population. Over the span of this Council's life, the increase in the number of persons of other than British or French origin has been equivalent to more than half of Canada's population growth; it has included a doubling of the native peoples and a tripling of those from Southeast Asia. Canadians take pride in these developments, but they must also be conscious of the need to provide adequate economic opportunities for ethnic minorities and to respond sensitively to the circumstances and special claims of their native compatriots.

Much has been said about the growth and size of government. Without discounting the increased involvement of the federal government, most of this growth has occurred at the provincial level, in response to the demands of Canadians for richer and more varied social services. The basic framework for these services is now well established, and the task for governments is not to dismantle them but rather to improve the delivery process and to contain cost increases that almost inevitably creep into programs that escape the efficiency-honing pressure of competition. Cost containment must be viewed in its full context, taking account of private as well as public expense, and in relation to legislated entitlements. Unemployment insurance expenditures, for example, are most effectively reduced by spurring economic buoyancy and the employment growth that accompanies it; health expenditures, by preventive efforts and resistance to excessive demands by health personnel.

While we have focused here, to a considerable degree, on distributive social issues, we must not lose sight of the fact that enlargement of the economic pie must precede its distribution. Renewed economic growth could well founder unless governments exercise prudent monetary and fiscal measures, including whatever is necessary to contain the re-emergence of excessive inflationary expectations. In many respects, the social programs now in place provide much of the automatic stabilization that is required to offset the cyclical swings of the markets. But there is also a discretionary role for governments that is necessary in setting a favourable climate for expansion in all parts of Canada.

We live in a turbulent world where scientific knowledge and new technologies are rapidly expanding and where the geopolitical ambitions and external trade practices of nations are often interwoven with domestic economic conditions. In looking to the future, how best can we steer the course ahead? Foremost, perhaps, is the need to keep our sights high and our aim at economic and social targets requiring the best conceivable effort. We are a medium-sized nation, but we are a nation that is envied and admired worldwide for the freedoms and the overall stability that it offers to its citizens. We have established, through many of the programs described here, that we are a humane and concerned people; now, we must establish that we are competitive, inventive, and productive. Here, the initiatives and enterprise of industry and labour will be crucial factors; for governments, probably the main concern will be to create a sound climate for growth; and, in the economic management of this nation, harmonization of effort between the federal and provincial governments will remain a prerequisite.

2 The Trading Scene

Since the Council's formation, dramatic changes have occurred in international commerce that have deeply affected Canada's situation as a medium-sized country that is heavily dependent on its external trade. The expansion of trade worldwide, the emergence of newly industrializing countries, and the quickening pace of foreign lending and investment have all been part of the process of global integration, in which the various activities contributing to each nation's balance of payments – merchandise trade, foreign borrowing and lending, direct aid, and decisions by multinational enterprises – have all become more interdependent. Indeed, in some areas of activity the distinction between international and domestic policies is becoming blurred. Government policies designed to provide industrial or regional stimulus, promote growth, or reduce unemployment are increasingly affecting trade and investment flows. Similarly, more and more large corporations, in planning new investments, are looking at global opportunities that may involve trade of intermediate goods for foreign or domestic assembly. A continuing issue for the future will be the need for nations to reconcile their international orientations and obligations with policies and regulations designed to meet domestic concerns, so as to achieve some degree of international harmonization in those areas where objectives and methods differ significantly across countries.

The Broader Context

The expansion of trade over the past three decades has been a worldwide phenomenon, attesting to the rapid transmission of knowledge, the diversification of consumer tastes, and the growth and mobility of populations. The rise in living standards and the veritable revolutions that have occurred in electronics, aeronautics, and satellite communications have effectively broadened human horizons and diminished what were once prohibitively costly spatial and temporal obstacles. Businessmen daily roam the world in search of new markets or of new, more cost-efficient production sites. Increased specialization on a worldwide scale has led to rising intra-industry trade flows and to a greater international diversification of commercial links.

There have been very substantial reductions in tariff barriers, following the Kennedy and Tokyo Rounds of negotiations held under the aegis of the General Agreement on Tariffs and Trade. According to one method of measurement, the average tariff on industrial products has fallen to about 6.5 per cent in the European Economic Community, to just over 6 per cent in the United States, and to a little more than 5 per cent in Japan; Canada's average rate is somewhat under 13 per cent. By 1987, as a result of the Tokyo Round, both the U.S. and EEC average tariffs will be under 5 per cent; Japan's, under 3 per cent; and Canada's, under 8 per cent. While the precise measurements themselves can be challenged, there is no question that tariff barriers to trade have come down and will decline further.

Paralleling these developments, however, and further demonstrating the interdependence of international and domestic considerations, has been the growing application of nontariff barriers in attempts to restrict trade. Some of these barriers are not covered explicitly by GATT regulations. Some were, when originally introduced, unintended – in the sense that they were designed to deal with domestic circumstances – but now, in the increasingly global context of trade, particularly in services, they are restrictive. Some are explicitly preferential, as in the case of domestic subsidies, export credits, and procurement policies. Others are deliberately protectionist, as in the case of import quotas or the negotiation of voluntary export quotas.

Indeed, despite successful tariff reductions, the certainty, stability, and security of market access among nations are being threatened by a host of selective nontariff, discretionary instruments embodied in domestic legislation that is often highly legalistic in application. At present, perhaps the single most important issue and the focal point for much of the debate within GATT has to do with "safeguards" (i.e., actions taken on an emergency basis, designed to prevent "serious injury" to domestic producers). It is here, in particular, that the multilateral nondiscriminatory principles of GATT confront the selective bilateral approach of some countries to trade, which is also embodied in many recent North-South and East-West trading and lending arrangements. It has been argued, for instance, that apart from domestic procurement policies, a major obstacle to the U.S. market now is "contingency" (or "standby") protectionism – i.e., a willingness by U.S. firms to petition for antidumping or countervailing duties as instruments to reduce foreign competition. It is unclear to what extent these subtle preferential and protectionist policies reflect deep-rooted structural developments or merely temporary defensiveness resulting from the difficult post-OPEC period of slow growth and high inflation. As more nations become highly urbanized and have similar profiles of manufacturing and service-sector employment, within each there is likely to be pressure for local preference and protection, as well as lobbying to obtain commercial advantage over foreign competition, particularly in times of slack economic activity. And just as national standards and national legislation are often necessary to harmonize commerce and ensure fair trade in the face of local self-interest, so international rules may well provide governments with the best defence against the protectionist lobbying of powerful, well-organized interest groups. In this connection, the role of GATT takes on added significance.

Some contemporary trade issues, however, now lie outside the present purview of that organization. These include trade in services and high technology, which certain countries (particularly the United States) would like to see incorporated into the purview of GATT. Other countries have taken the view that bringing these issues under new GATT provisions now would entail institutional changes that could result in some hardship and that it is better to wait for a more complete recovery of world trade before tackling them.

Many of the preferential and protectionist trade barriers in both the industrialized and the developing nations have been applied mainly against final goods; as a result, intermediate goods have been commanding a growing share of the expanding global trade. Domestic and foreign investment is increasingly being directed to assembly operations that import some or most of the component parts, thereby further increasing the process of global integration while simultaneously creating domestic employment and expertise. Most governments have actively promoted this process. Many are also directly or indirectly major purchasers of goods or are intermediaries through which loans – often "tied" – are negotiated. Their involvement introduces a new dimension into international commerce, especially if strategic or geopolitical considerations are in play.

These are only some of the international developments that pose important policy issues for the future. They are a product of past economic cooperation that has given rise to a far more integrated world economy and, with the spatial shifts of activity that have occurred, a high interdependence between trade, investment, and international finance. For most industrial countries, the application of most-favoured-nation tariffs *per se* is no longer a major constraint to trading activity; however, preferential industrial strategies and the exercise of nontariff barriers do constitute obstacles. In the years ahead, many issues must be resolved: how to bring the newly industrialized countries into full compliance with GATT's most-favoured-nation treatment; how to steer commerce in the relatively uncharted waters of the trade in services; and how to meet the OECD's commitment to "positive adjustment" policies aimed at speeding up and fulfilling the domestic realignment of productive resources, in keeping with more open trade, aid, and investment.

Clearly, future debates about trade policy will involve rather different questions from those which dominated in the past 35 years – questions touching on basic concerns with respect to the social and even, in some instances, cultural interests of nations. Further progress in the elimination of barriers to world commerce will require a readiness on the part of governments to permit international machinery to impinge upon the internal processes of policy-making in various ways. More and more, those championing freer trade may argue for global rules and mechanisms to guide national economic and social management; and one can be sure that, more and more, there will be strong domestic political opposition in the name of national self-interest. The challenges will be daunting.

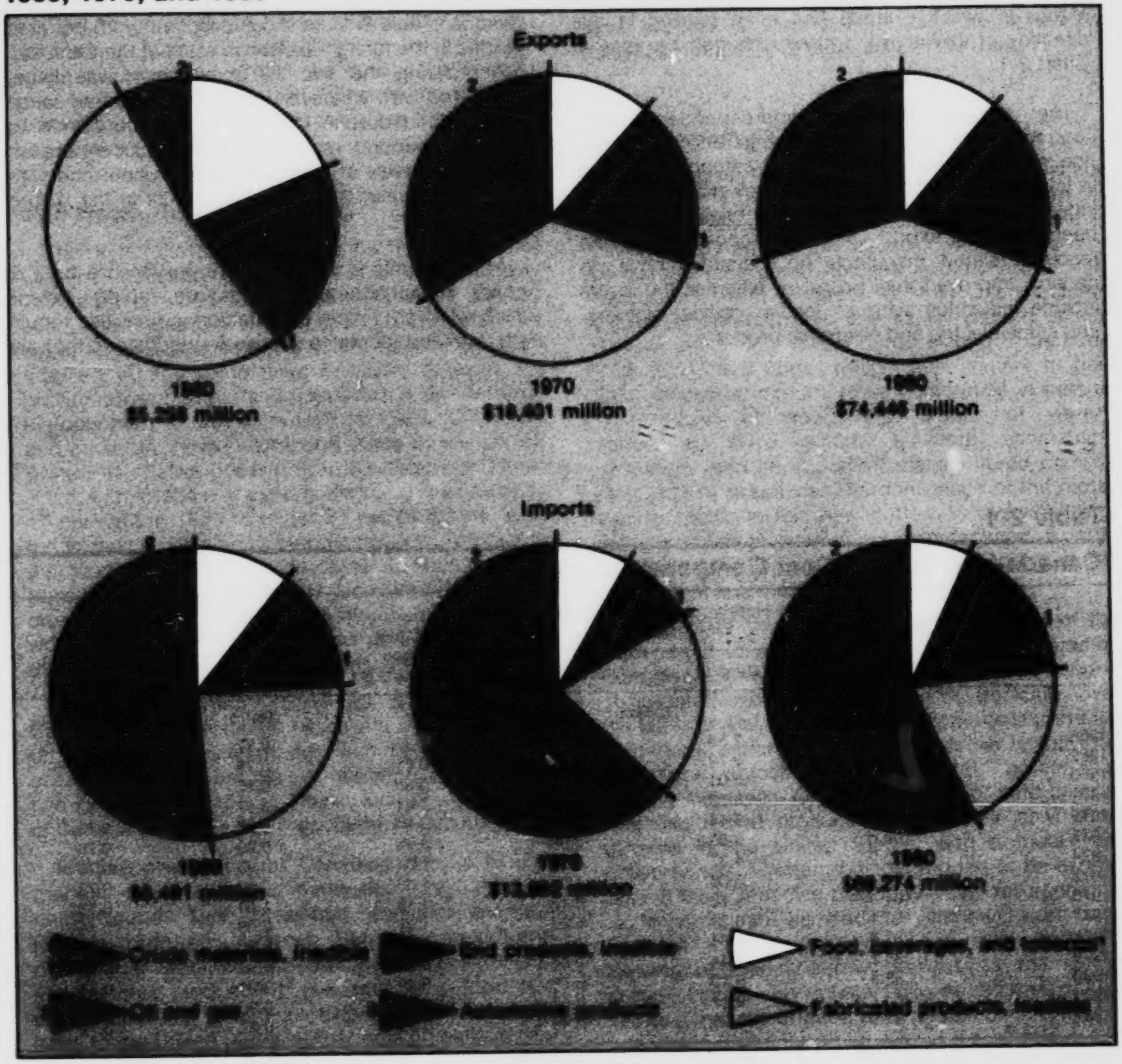
The Changing Trade Picture

The last two decades have also seen a very significant change in the structure of Canada's balance of payments. Our traditional position as a nation that relied mainly on the exports of primary and semifabricated goods and whose net indebtedness on the current account was offset by the importation of risk capital from abroad, has altered. Today, thanks in part to cyclical factors but also in part to basic structural changes in the economy, Canada enjoys a large merchandise surplus, and a growing opinion among financial circles is that it will soon become an overall net lender of capital abroad.

Whereas traditionally Canada's comparative advantage in primary goods – farm commodities, minerals, forest products, and so on – helped to support a somewhat costly policy of import substitution in the protected manufacturing sector, in recent times this rather simple pattern has become much more complicated. World trade in primary resources has been growing relatively slowly, compared with that in manufactures: the commerce in food and raw materials among market economies today is approximately 2.5 times as great, in real terms, as it was two decades ago whereas the corresponding figure in

Chart 2-1

Distribution of Exports and Imports, by Commodity Group, Canada, 1960, 1970, and 1980



1 Including live animals and feed.
SOURCE Based on data from Statistics Canada.

respect of manufactured goods is about 5 times. Moreover, the importance of the secondary industries and the rapidly proliferating tertiary activities in providing employment and income to Canadians has reached such a point that any inefficiencies are bound to generate a high cost to the nation. For quite some time, therefore, part of the discussion in respect of improving economic performance has been about how to move Canada's manufacturing sector from its relatively small-scale, domestic orientation to a more viable condition that will enable it to match the output of other countries in both quality and price. The extent to which Canada has been moving in this direction in its imports and exports can be seen in Chart 2-1.

The growing worldwide interdependence has spurred substantial structural change and specialization in Canada, with some product categories gaining in importance and others losing their market shares; indeed, even within product categories there have been offsetting export gains and import losses. The resource-related manufacturing industries have, in general, improved their positions, whereas the losers include industries such as leather goods, clothing, and some electric and electronic products.

Productivity developments have also affected Canada's trade position. During the 1970s Canadian manufacturing workers realized dramatic wage gains, compared with their U.S. counterparts. At one point during the decade, Canadian wages substantially exceeded those of U.S. workers (expressed in either U.S. or Canadian dollars), although average productivity levels in Canada were notably lower. The devaluation of the Canadian dollar subsequently restored some of the traditional relationship, but in terms of overall manufacturing productivity, labour compensation remained considerably higher in Canada (Table 2-1). In short, despite the 20 per cent decline in the foreign-exchange value of the Canadian dollar during the late 1970s – which was large, compared with whatever tariff reductions had taken place – and despite the fillip that this imparted to Canadian exports, many Canadian producers are left with lower levels of output per person-hour and with higher unit costs and prices than exist in the United States.[1]

In a dynamic world, therefore, in which a host of newly industrializing countries are rapidly moving from relatively simple manufacturing activities requiring unskilled labour to processing industries that are

Table 2-1

Canada-U.S. Labour Cost Comparisons, 1968-82

	Exchange rate ($Can/$U.S.)	Hourly manufacturing wages ($Can)		Relative wages (Canada/U.S.)	Relative total compensation (Canada/U.S.)	Productivity comparison (Canada/U.S.)
		Canada	United States			
	(Cents)	(Dollars)			(Ratio)	
1968	92.8	2.58	3.24	0.80	0.77	0.68
1969	92.9	2.79	3.44	0.81	0.78	0.71
1970	95.6	3.01	3.51	0.86	0.83	0.72
1971	99.0	3.28	3.61	0.91	0.87	0.73
1972	101.0	3.54	3.78	0.94	0.89	0.73
1973	100.0	3.85	4.08	0.94	0.89	0.73
1974	102.2	4.37	4.31	1.01	0.95	0.76
1975	98.4	5.06	4.89	1.03	0.96	0.73
1976	101.4	5.76	5.12	1.13	1.04	0.73
1977	94.1	6.38	5.98	1.07	0.99	0.75
1978	87.7	6.84	7.04	0.97	0.93	0.75
1979	85.3	7.44	7.84	0.95	0.90	0.75
1980	85.5	8.19	8.50	0.96	0.91	0.74
1981	83.4	9.17	9.58	0.96	0.90	0.73
1982	81.0	10.26	10.49	0.98	0.91	0.72

SOURCE Based on data from P. Wonnacott and R. J. Wonnacott, "Free Trade Between the United States and Canada Fifteen Years Later," *Canadian Public Policy* (October 1982):417; and unpublished data from the U.S. Department of Labor.

more capital-intensive and more technologically advanced, Canadian producers must dedicate themselves to the task of containing costs and increasing their productivity in order to remain competitive. It is not just that the hourly output of U.S. workers is so frequently higher than that of their Canadian counterparts; it is also that the productivity of similar workers in Japan and in other, less advanced Asian countries is rapidly catching up. Indeed, a recent survey of technology imports into the United States showed that the geographic sources from which technology is imported "go far beyond the countries that come to everyone's mind"; the reasons most frequently given for using foreign-made machinery were: first, its quality; second, its price; and third, its availability.[2] Therein the competitive challenge for Canadian firms no less than for U.S. enterprises.

The North American Nexus

The United States, traditionally the "locomotive" of western industrial growth, is now more closely integrated in world trade relations than it was 30 years ago. Indeed, over the period U.S. exports and imports, as a proportion of GNP, have more than doubled. At the same time, however, because the growth rates of output and population in the developing countries, as well as output per capita in Europe and in Japan, have outstripped those of the United States, its relative position in world trade has diminished, with its share of exports dropping from close to 17 per cent in 1955 to under 11 per cent now. With the widening diffusion of high-technology initiative in the world and with the increase in technological transfers and in the number of goods being produced on a global scale, some expect that the U.S. share of world exports will continue to decline gradually throughout the balance of this century.

These developments serve as a backdrop to Canada's trade relations, which are largely focused on the North American market, with the United States accounting for 70 per cent of our imports and about two-thirds of our exports. This includes a rising share of Canada's trade in fully manufactured products.

In 1960 over half of all Canadian exports to U.S. markets were fabricated materials – i.e., semiprocessed goods, such as lumber, newsprint, chemical products, and refined metals. Between one-fifth and one-quarter were crude materials like potash and mineral ores, and about one-tenth were food and related products. Less than 10 per cent of Canada's sales to the United States at that time comprised fully manufactured items. Today, such items are the single most important category of exports, accounting for roughly 40 per cent of the total in a typical year, whereas fabricated materials represent about 35 per cent, crude materials under 20 per cent, and farm produce no more than 5 per cent.

On the import side, too, the share of manufactures has risen, though less strongly and from a much higher starting point. In 1960 manufactured goods already accounted for more than half of all Canadian purchases from the United States; that share has now risen to two-thirds. Our receipts of fabricated materials have also fallen a fraction in proportional terms, from around one-fourth to less than one-fifth of the total; purchases of crude materials have remained virtually constant at less than one-tenth; and imports of food and related products have dropped marginally to 6 per cent of the total.

The Automotive Trade

The integrative effect of the 1965 U.S.-Canada Automotive Agreement altered the structure of commerce between the two countries quite markedly – particularly on the export side, where Canada is concerned – by greatly increasing the share of total transactions that consists of fully manufactured goods. In contrast with the earlier pattern, where Canada paid for a broad range of goods imported from the United States mainly with primary or partially processed exports (thus conforming in part to the "hewer of wood and drawer of water" caricature), there is now a more symmetrical exchange, with an important manufactured component in both directions. The dominance of the motor vehicle sector in this new pattern is overwhelming, with two-thirds or more of our manufactured exports, and about half of our manufactured imports, being made up of automotive products.

In terms of the trade balance, both sides of the ledger tend to rise or fall in tandem; that is, when Canadian automobile exports rise, so too do imports of automotive parts, and vice versa. Ironically, over the latter part of the recent recession, the importance of trade in automotive products relative to the total commerce across the Canada-U.S. border has actually increased. Originally, the major auto companies decided to produce most of their down-sized vehicles in the United States, with a more-than-proportionate number of bigger models to be assembled in their Canadian plants. With the resurgence in North American demand for standard-sized cars (brought about by lower gasoline prices), Canadian exports of standard-sized vehicles to the United States climbed very substantially, as did the complementary imports of parts and components from U.S. factories.

Given the weakness of the North American automobile industry during the recession and the extent of Japanese competition in recent years, concentration on the automotive sector in Canada-U.S. trade may create a potential for vulnerability. Import penetration from outside North America poses serious challenges for the automobile industry, and much of the apparent resiliency of the domestic automotive market rests, in fact, on the application of "voluntary export quotas" by the Japanese on their shipments to the United States and Canada. That should not be regarded as a permanent condition: Canada's automotive industry, along with that of North America generally, must continue to improve its basic productivity and the quality of its products if it is to remain competitive.

Other Trading Links

The defence equipment industry has been another source of integrated manufacturing trade with the United States. The original Canada-U.S. defence-sharing agreement, signed in 1959, is a cornerstone of Canada's NATO commitment. Along with the Defence Industry Productivity Program,[3] it has stimulated the development, production, and export of highly sophisticated defence and aerospace equipment over the years. Some of this shows up in the automotive trade figures – those for military vehicles, in particular – and also in those for aircraft and parts. In addition, there is a growing trade in highly specialized engineering equipment and gear for military use, much of which is on the leading edge of the newest technology, with a potential for much wider application.

Significant attention has recently been directed at the development of trade in high-technology products – especially telecommunications apparatus and electronic office equipment (including computers of all kinds). Despite the inroads of consumer electronic products from Japan and Southeast Asia into the Canadian market and the moderate success experienced overseas by Canada's manufacturers of industrial telecommunications equipment, this country's principal export market for "high-tech" products remains the United States. At present, Canada is, as could be expected, mainly an importer. In 1982, for example, over 4 billion dollars' worth of telecommunications equipment was purchased from U.S. sources, while sales to that country totaled about $1.5 billion. Over the past few years, however, U.S.-bound exports in both of these categories have risen more rapidly than imports. On the broader front of technology-intensive products, Canada has traditionally had a bilateral deficit with the United States; however, although that deficit currently stands at almost $10 billion, it has shrunk as a proportion of the two-way trade in recent years.

Intracorporate Trade

Notwithstanding the strengthening of Canadian exports of manufactured goods, the United States has been able to treat the Canadian consumer and industrial market practically as extensions of its own within the North American context. Where circumstances have led to U.S. direct investment in Canadian production facilities – this decision often being related not only to integrative factors but also to Canada's import protection – there has tended to develop a symbiotic trade relationship between Canadian subsidiaries and branches of the parent operations. The importance of such exchanges is one of the forces that are contributing to further consolidation of the interlocking North American economy.

Much of the commerce across the border is, in fact, intracorporate movement of goods between units of the same firms rather than the usual sort of arm's-length transaction between unaffiliated concerns. This has implications for the competitiveness and market opportunities of Canadian firms, for investors and financial intermediaires, and even for the tax base of government at both the federal and the provincial levels.

The interrelationship of direct investment and trade is demonstrated by the highly significant role that foreign-controlled firms play in Canada's imports. For example, a recent study has revealed that 87 per cent of all Canadian purchases from the United States in 1978 were made by U.S.-controlled enterprises.[4] To determine the extent of intracorporate imports, the Department of Industry, Trade and Commerce periodically undertakes a survey of about 300 of the larger foreign-owned companies (with assets over $5 million) operating in Canada – a group that accounts for about half of all foreign-owned firms in terms of sales.[5] According to that survey, for selected industries the proportion of imports from the United States by foreign-owned Canadian firms that are essentially intracorporate in nature rose from 67 per cent in 1965 to 79 per cent in 1979 (Table 2-2). Among the industries surveyed, intracorporate imports in 1979 ranged from 28 per cent for the food and beverage industry to 87 per cent for the gas and oil industry. The dimensions are similar in the export trade. Overall, intracorporate exports as a share of total exports amounted to 63 per cent in 1965 and to about 80 per cent throughout the 1970s. As with imports, much of the increase in intracorporate exports in the 1960s resulted from the Canada-U.S. Automotive Agreement.

Thus intracorporate trade continues to play a considerable role in the Canada-U.S. economic relationship, and it has distinct implications for this country's competitiveness and growth potential, as

Table 2-2

Canada-U.S. Intracorporate Trade, Selected Years, 1965-79[1]

Proportions of all import and export trade with the United States that is between foreign-owned Canadian subsidiaries and their parent companies

	1965		1970		1975		1979	
	Imports	Exports	Imports	Exports	Imports	Exports	Imports	Exports
	(Per cent)							
Mining and primary metals	77.9	82.4	81.3	84.1	71.3	72.8	81.2	70.3
Gas and oil	80.8	62.5	72.9	68.2	87.7	51.6	87.3	53.8
Machinery and metal fabricating	79.3	95.2	79.3	96.1	78.1	70.3	80.3	76.8
Transportation equipment	67.0	59.0	76.0	91.7	76.1	94.4	81.5	93.5
Electrical products	69.7	80.0	64.2	54.5	64.7	75.4	65.0	70.3
Chemical products	55.0	34.4	60.4	64.9	67.2	50.8	68.8	80.6
Food and beverage	46.3	62.5	42.2	66.1	37.1	59.6	27.7	30.8
Pulp and paper	21.9	51.4	28.6	54.5	28.1	59.0	58.0	52.1
Other manufacturing	64.9	67.9	69.8	65.2	72.3	72.5	83.9	81.8
Wholesale trade	80.6	94.8	78.5	90.6	83.1	92.1	76.5	90.6
Other nonmanufacturing	35.0	100.0	60.0	70.0	75.2	100.0	68.9	46.2
Total	66.9	63.0	73.3	81.6	74.5	80.1	78.9	81.3

1 Based on a sample of larger foreign-owned firms accounting for approximately half of the sales volume of all foreign-owned firms in Canada.

SOURCE Department of Industry, Trade and Commerce, *Foreign Owned Subsidiaries in Canada*, Ottawa, various issues.

well as for our perception of foreign direct investment. Certainly, the intracorporate trade that is associated with the auto pact has raised the Canadian automotive industry's productivity, with the reduction of import barriers on both sides of the border enabling Canadian plants to specialize in certain lines and to achieve scale economies through expanded production runs. Moreover, the intracorporate relationship often assures Canadian subsidiaries of relatively stable markets for their exports and enables them to draw on the financial strength and the marketing and technical expertise of parent firms. Most of the new technology adopted by Canadian firms through imitation or diffusion originates abroad, and much of it involves intracorporate transfers. As we observed in *The Bottom Line*, "in sum, the foreign-controlled corporation is one of the fastest and most effective channels through which new, sophisticated, and expensive technological know-how is imported into Canada. Although this means that less R & D is done in Canada than might otherwise be the case, it also means that significant technological benefits accrue to Canada."[6]

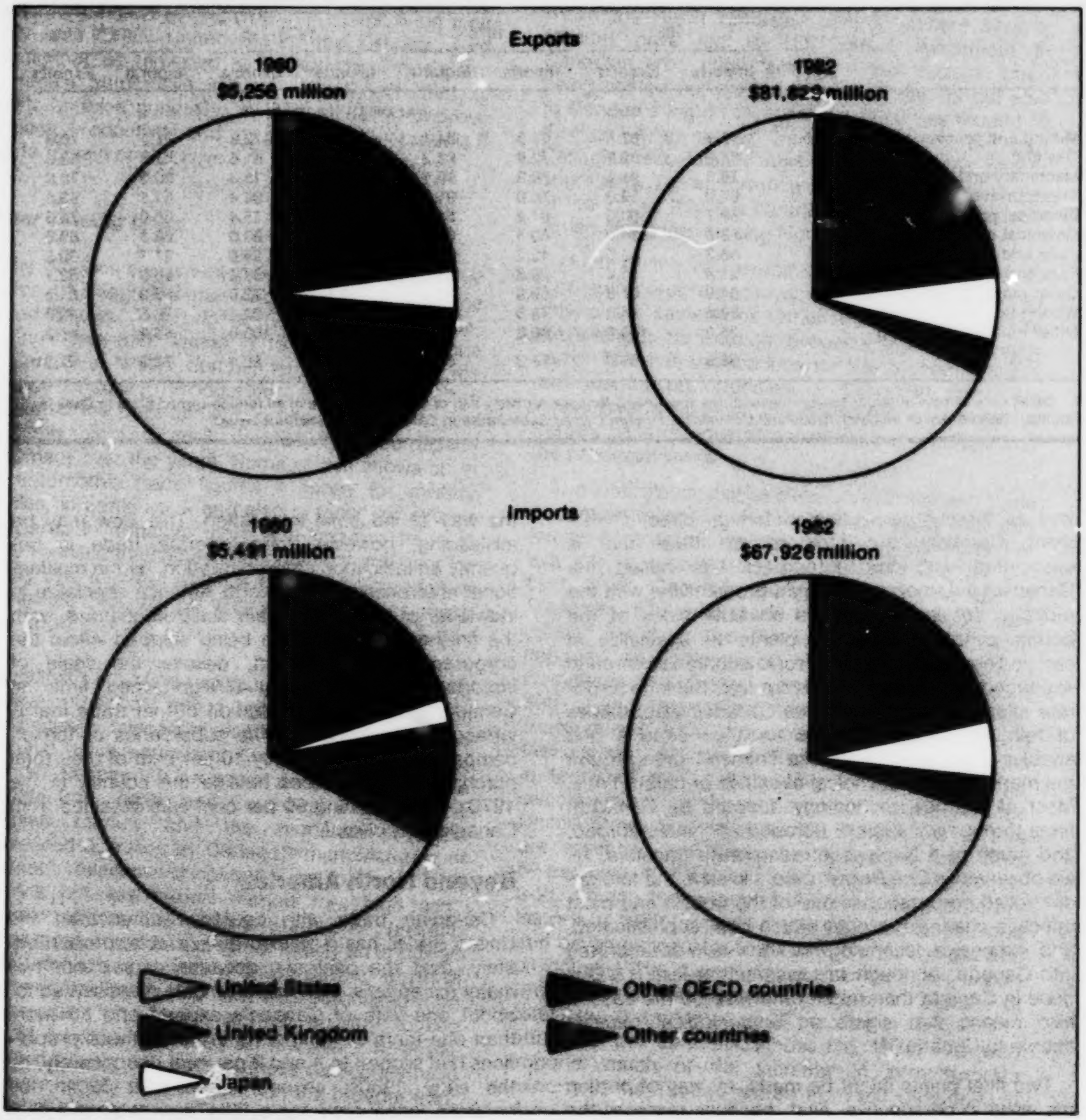
Two final points might be made, by way of putting the issue in perspective. First, because many of the intracorporate imports are of finished goods rather than raw materials or partially processed items, it may appear that, in some cases at least, the subsidiaries of foreign firms perform something akin to a wholesaling function that does not involve much in the way of industrial integration. This view may be misleading, however. Intracorporate trade is frequently an indication of specialization, as the multinational enterprises across North America specialize in individual products and gain scale economies, with the finished products then being shipped within the corporation. And, second, despite the scale of imports from abroad by foreign-owned firms in Canada and the high proportion of that trade that is intracorporate in nature, the subsidiaries of foreign companies still derived only 40 per cent of their total purchases from sources outside the country in the 1970s; the remaining 60 per cent was obtained from Canadian suppliers.[7]

Beyond North America

Canadian trade with countries other than the United States has remained quite stable, proportionately, over the past two decades or so, with two major exceptions: first, whereas Britain accounted for about one-sixth of Canada's exports and for more than one-tenth of its imports in 1960, these proportions had slipped to 4 and 3 per cent, respectively, by the early 1980s; second, trade with Japan, by contrast, accounted for a little over 3 per cent of Canada's exports and 2 per cent of its imports, respectively, in 1960, but that situation subsequently shifted steadily, and by the early 1980s Japan accounted for over 5 per cent of Canadian exports and imports (Chart 2-2).

Chart 2-2

Distribution of Exports by Destination and Imports by Origin, Canada, 1960 and 1982



Source Based on data from Statistics Canada.

The decline in the importance of Anglo-Canadian trade began with a shrinkage in the margin of advantage provided by the "British preference" (B.P.) tariff schedule as overall import duties came down in the successive rounds of GATT negotiations. It accelerated with Britain's entry to the European Economic Community in 1973, which not only terminated benefits for Commonwealth members under the B.P. system but forced Canadian exporters (like those of other non-EEC countries) to pay the Community's "common external tariff," whereas EEC suppliers had duty-free access to the British market. And, of course, the poor performance of the British economy in the 1970s did nothing to enhance mutual trade.

As for Japan, industrial development has been such as to create an immense demand for raw materials and other primary commodities that Canada is well equipped to offer, and to yield spectacular improvements in the range and variety of Japanese manufactured exports. Canadian exports to Japan fall mainly in the category of crude materials, as has long been the case, with fabricated materials and farm produce occupying the second and third positions, respectively; fully manufactured goods represent a miniscule 3 to 4 per cent of all Canadian sales to that country. On the other hand, the goods that Canada buys from Japan are overwhelmingly in the end-product category, with motor vehicles and electronic equipment forming the lion's share of this trade.

A handful of other states of eastern Asia – notably South Korea, Taiwan, Hong Kong, and Singapore – are now following Japan down the industrialization path, and in consequence they too are strengthening their positions as markets for Canada's exports and as sources for its imports. Although their combined population is about half that of Japan and although their trade with Canada is relatively minor in comparison with that provided by Japan, during the 1970s the growth of their domestic economies and their trade was even stronger than Japan's. On the export side, these markets are rather favourably disposed towards Canada's manufactured products; one-fifth or more of our sales to three of these four countries are end products; even the least receptive state (Taiwan, where Canada's exporters are hampered by the lack of Export Development Corporation financing, owing to Canada's diplomatic policy vis-à-vis China and Taiwan) accepts at least twice as high a proportion of manufactured imports from Canada as the Japanese do. On the import side, Canadian purchases from these countries are mainly in the fully manufactured category, except that the goods shipped are somewhat less advanced technologically – mainly clothing, footwear, sporting goods, and small consumer appliances – than are imports from Japan.

In combination, the extraordinary Japanese performance, the emergence of new major exporting countries (South Korea, Taiwan, Hong Kong, and Singapore), and the evidence of similar (though as yet fairly localized) industrial growth in other nations of Southeast Asia (Malaysia, the Philippines, Indonesia, and Thailand) have encouraged the view that, in the twenty-first century, the Pacific Rim could well be a focus of economic activity and trade comparable to the North Atlantic basin. Given the political obstacles to large-scale trade interdependence with the socialist countries and territories of that region (China, Siberia, Mongolia, North Korea, and the Indochinese peninsula) at the moment, to say nothing of their relative poverty, trade beyond the region is the main option available to these market economies, if they are to continue to move ahead. Greater Canadian interest in developments around the Pacific Rim is therefore warranted.

If one encompasses in the Pacific Rim the western United States (including Alaska and Hawaii), Mexico, the Central American republics, the nations of western South America (Colombia, Ecuador, Peru, and Chile), New Zealand, Australia, and all the countries of eastern Asia (including China), one has an entity to which Canada sold almost 18 billion dollars' worth of goods in 1982 and from which it purchased close to 14 billion dollars' worth. These figures account for around 20 per cent of total Canadian exports and imports – a fairly impressive proportion. It has to be pointed out, however, that nearly half of all that Pacific trade was, in fact, with the western United States, and one-fourth was with Japan. Canadian trade with the other Pacific Rim countries amounted to just one-quarter of its trade with the region as a whole – or about 5 per cent of its global commerce.

Leaving aside the decline in commerce with Britain, the other western European nations provide a market for almost exactly the same proportion of Canadian exports today – and are the origin of a virtually identical share of Canadian imports – as was the case 20 years ago. Nor has the structure of the trade changed very much, except that European purchases of Canadian farm commodities are relatively lighter, and imports of manufactured goods relatively heavier, than was the case then. The relative weakness of our farm exports is very largely a result of the EEC's "common agricultural policy," while the strength in manufactures reflects the improved competitiveness of Canadian secondary industry and, to some extent, the internationalization of corporate logistics in some large firms. The major items in Canada's exports to Europe in this category are telecommunications equipment, aircraft engines and parts, office machines and equipment, some types of machinery, and certain lines of clothing. On the import side, the only structural shift over the past 20 years has been a very recent emphasis on Canadian purchases of North Sea oil from Britain.

Trade with the rest of the world presents no particularly dramatic developments. Canada sells extremely large volumes of wheat and other grains to the Soviet Union and China when their harvests are poor; indeed, the eastern European countries have partially replaced our more traditional grain markets in western Europe and elsewhere. To date, these communist nations evidently have little interest in other Canadian products, however, and they have little to offer for Canadians to purchase, so that the trade is essentially one-dimensional. The OPEC countries in the Middle East and some African nations have provided a market for Canadian-made machinery, engineering equipment and services, and some other commodities, but on the whole the trade flows have been modest.

Latin America keeps showing promise, and countries like Mexico and Brazil became quite attractive as markets, and enterprising as suppliers, for a time in the 1970s. But the recent financial crises in both countries and reduced oil revenues in Venezuela have somewhat diminished trade opportunities in three of Canada's more promising trading partners. Thus, while Latin America, with a combined population greater than that of the United States, seems certain to offer increased scope for Canadian trade over time, it has yet to move from promise to much in the way of actual fulfilment.

The "Invisible" Trade

Of growing international importance in the 1980s and 1990s will be the international "invisible" trade in services. While such trade was equal to less than one-third of the value of merchandise trade worldwide ($620 billion vs. almost $2,000 billion) during the 1970s, it grew by 17 per cent annually, compared with 6 per cent for the merchandise trade.[8] In 1980 the United States, Britain, and France had large surpluses from their "invisible" trade, while Japan, West Germany, and Canada had large deficits. According to the federal Task Force on Trade in Services, receipts on the service account in 1981 were just under $15 billion, compared with close to $85 billion for exports of goods.[9] Moreover, if the measure is confined to "tradable" services (which comprise three categories – travel, freight and shipping, and "other" – with interest, dividends, and miscellaneous investment income being excluded), receipts came to less than $12 billion that year.

Most Canadian travel is between domestic locations. For example, 90 per cent of the roughly 120 million trips made in 1981 were to Canadian destinations.[10] But, of the $15.5 billion that was spent, only 60 per cent was retained in the domestic economy; trips to the United States and elsewhere took 23 and 15 per cent, respectively (close to $5 billion), of the travel expenditures, while travel receipts from foreigners visiting Canada amounted to almost $4 billion. Deficits on the travel account have been a feature of Canada's services trade for a long time. They grew rapidly in the early 1970s, peaking in 1978. After the depreciation of the Canadian dollar, they declined to the current level of around $1 billion annually – two-thirds of that amount being derived from travel between Canada and the United States.

Freight and shipping receipts by Canada exceeded $4 billion in 1981, showing a very slight surplus over payments for comparable purposes. Throughout the past decade, this sector of the services account has been virtually in balance, with slight shifts seeming to follow fluctuations in the goods-trade cycle.

The catch-all category of "other services," which covers a variety of business and personal services as well as government transactions, accounted for most of the tradables deficit in 1981, with receipts and payments approaching $4 billion and $6 billion, respectively. This part of the services trading account has seen a continuing and rising deficit for 30 years. When the "government transactions" segment is excluded, however, the increase has remained almost in line with the growth of the economy as a whole.

The "other services" category encompasses most of the international transfers that many say will grow in volume and significance as today's leading industrial countries become tomorrow's postindustrial societies. It includes a wide variety of activities: consulting and other professional services; management and administrative services; insurance business; scientific research and product development; royalties, copyrights, and trademarks; advertising and sales promotion; equipment rental; and franchises and similar rights. It is widely predicted that by the first decades of the next century if not earlier, the most advanced nations will concentrate largely on the sale abroad of these sorts of intangibles, many of which incorporate sophisticated technical and professional expertise, while the less advanced countries will rely heavily on exports of standard manufactured goods. Given that Canada is, in some ways, an "in-between" country, it is useful to examine how its receipts and payments in some of these fields have been behaving, by comparing their "export orientation" (the value of receipts relative to domestic production) in these respects with their "import penetration" (the ratio of payments to domestic consumption).

The Task Force's assessment showed that transportation and storage had had the highest export orientation for Canada but that this trend had been declining. It may decline further as a result of the recent deregulation in the U.S. airline, rail, and trucking industries. In business services, export orientation and import penetration had fluctuated considerably over the years and showed no clear trend. In fact, the only really interesting development was in communications services, where both export orientation and import penetration had grown, the latter somewhat more rapidly than the former. Altogether, the list presents a less-than-exciting indication of Canadian export prospects in this regard, though it has to be said that the data are extremely scant and that the extent of disaggregation is insufficient for detailed analysis.

Nevertheless, Canada could make inroads in this area by encouraging the export promotion of financial, managerial, engineering, and scientific services abroad, particularly in the OPEC area and in the newly developing countries where there is a potentially strong demand for them. Canadian banks, for instance, have greatly expanded their presence and loan operations abroad; major Canadian real estate firms are also active, particularly in the United States; and Canadian telecommunications firms are well represented and active in the Middle East. There is, therefore, substantial scope for vigorous promotion of Canadian exports of services, since that is an area where Canada has, or should have, a comparative advantage vis-à-vis many other countries.

Tariff Cuts and Nontariff Barriers

Because of the tariff barriers imposed by Canada against goods made elsewhere and those erected by other countries (particularly the United States) against its manufactured goods, Canadian producers in the past tended to concentrate on the small domestic market and to operate at a relatively low volume and at size levels that were less than fully efficient. The combination of this relative inefficiency and foreign tariff barriers limited the ability of Canadian manufacturers to export. In addition, because the United States forms a much larger market, the prices of many internationally traded manufactured goods are determined there, and Canadian exporters must match these prices on foreign markets. As a result, they directly or indirectly wind up paying the U.S. tariff. In the case of many similarly priced manufactured imports, Canadian consumers pay the Canadian tariff to the Department of National Revenue; while this is merely a domestic transfer, it does not compensate Canada for the losses on those exports for which its producers effectively pay the U.S. tariff.

The combination of the U.S.-Canada Automotive Agreement and the mutual reduction of tariff barriers has been of particular benefit to Canadian manufacturers, and it has contributed to the rising proportion of Canadian factory shipments that is exported – from less than one-fifth in 1966 to almost one-third now. Over the same period, import penetration from abroad increased from around 20 per cent of the domestic market to more than 30 per cent.

Canada has undertaken a series of important reforms affecting the way in which the tariff is administered. They include the adoption of a common international system for classifying goods for tariff assessment and a change in the valuation method of imports (from "fair market value" to "world market price") for the purpose of levying duties, with offsetting tariff adjustments to compensate for the expected loss of protection. These measures are expected to make the tariff a much more "transparent" instrument of protection.

Some worry that the weak performance of the western economies in the wake of the recent recession and the prospect of continuing high unemployment will lead governments to try to slow down, or even reverse, the reductions in their tariff barriers. Such an amendment to the agreed arrangements would require the approval of the whole GATT membership, which means that it could only occur in an atmosphere of crisis, being perceived perhaps as the sole means of holding the system together in the face of widespread determination to "do what is necessary" for the survival of domestic industries. Time will tell how real the threat may be.

Of special concern is the growth in nontariff barriers that has accompanied the recent period of slower growth – barriers put up by governments that increasingly see foreign goods as a threat to jobs in the domestic economy. These obstacles to trade take a variety of forms: quotas, voluntary export restraints, orderly market arrangements, administrative delays, government procurement policies, and domestic-content rules are part of the protectionist armoury, but measures to promote exports (such as export subsidies and "dumping" of goods below cost) are also used for reasons of immediate national economic self-interest. While great ingenuity has been shown in dreaming up deliberate nontariff hurdles to trade in recent years, many elements of protection are not so deliberate, such as the complicated rules for electrical standards and pollution control that some countries have set up and that make it difficult for foreign suppliers to enter their markets.

Measures such as these are particularly evident in agriculture, where there has been excess domestic supply in response to high prices, with the result that the Third World has become a convenient dumping ground for the food surpluses of North America and Europe. With respect to steel, North American producers (including Canadian ones) have filed antidumping suits against European, Japanese, and South Korean steel products. In 1982 the U.S. government applied import quotas on carbon steel products from Europe and elsewhere, including Canada; this year, it adopted similar restrictions on specialty steel. In textiles and clothing, the Multi-Fibre Arrangement (MFA), adopted in 1974 to give poor countries guaranteed and growing access to western markets, was renegotiated in 1978 and extended in 1982, with "safeguards" that allow for the negotiation of bilateral arrangements favouring the rich nations over the poor. The MFA now contains more than 3,000 quotas for different countries and different products; one commentator has written that the MFA, which had been "introduced as an instrument to help poor countries develop . . . . has put them in handcuffs."[11] In the automobile industry, as noted above, protectionism is widely practiced. In the United States, the Congress is considering local-content rules that would effectively curb imports of Japanese and, perhaps, Canadian vehicles. Canada has been no less guilty, having used administrative delays in Vancouver to pressure the Japanese into lowering their "voluntary" export quotas. Europe has been even more blatantly protectionist against imports of Japanese automobiles, but no more so than some of the newly industrializing countries that are trying to develop their own auto industries.

One of the most favoured and most highly visible nontariff barriers is the quota, which may be either "voluntary" or mandatory. Quotas usually place an upper limit on the number of units of a particular good (generally defined fairly broadly, so that price and quality can vary considerably within a category) that can be imported. Automobiles, textiles, clothing, footwear, and some agricultural products (turkeys, cheese, chickens, and eggs) are important examples of products that have been subject to quotas.

Quotas have proven to be an expensive means for cushioning workers against the threat of foreign competition. In particular, the total wages earned by workers protected by this means typically fall well short of the costs imposed on consumers through higher prices. Moreover, quotas can lead to resource misallocation even within the protected industry. For example, import quotas were found to have resulted in much stiffer competition in the more profitable high-value-added, quality component of the clothing industry; at the same time, they encouraged Canadian producers to shift towards the lower-profit, low-quality end of the market.

Except for quotas, in many cases nontariff barriers are not readily amenable to trade liberalization because they are frequently qualitative aspects of a nation's domestic policy arrangements (or, in any event, are made to appear so) rather than straightforward proportional taxes on the value of the goods crossing borders, as are import tariffs. Understandably, governments have shown themselves reluctant to let any international arbiter decide whether or not they should be allowed to introduce a particular health regulation, for example, even if it can be pointed out that a trade obstacle is implicit in the proposed measure.

Thus, despite success in lowering tariffs, to a greater or lesser degree all western countries have been guilty of seeking to maintain protectionism. With the levels of import duties falling still further under the Tokyo Round, in many respects nontariff barriers are now a greater threat than tariffs to world trade and to the economic well-being of all nations, including the developing countries. It has been estimated, for instance, that by 1982 "the U.S. product sectors protected overtly by nontariff barriers – when weighted by each sector's share of total consumption in manufacturing – covered 34 per cent of the market for American manufacturers. In Japan the comparable figure was 7 per cent; in Canada, 10 per cent; in West Germany, 20 per cent; in France, 32 per cent."[12] This does not include other interventions by governments in the form of tax expenditures, subsidies, or barriers under the pretext of national security. Needless to say, however, the scale and effectiveness of these barriers in protecting each country's producers is in no way measured by such calculations.

An important requisite in discussing and evaluating nontariff barriers in international fora is that all participants be aware of the magnitude and impact of such barriers, so that sensible bargaining can take place. A number of indicators could be useful: the tariff equivalent of the nontariff barriers; the impact on quality, costs, and competition in the affected industries; and an estimate of the economic costs and benefits. Obtaining these measurements is not likely to be an easy task, as evidenced by the scarcity of such information at present. We therefore believe that Canada should make strenuous efforts to encourage the classification and quantification of nontariff barriers (both its own and those of its trading partners), so as to be fully prepared for the future stages of the multilateral negotiations on these obstacles.[13]

Nontariff barriers are now coming under the scrutiny of GATT, and they will be high on the agenda of future meetings of the signatories to that accord. Throughout the 1980s the task for GATT member nations will be to come to grips with these obstacles to trade and to facilitate their negotiated removal. Of first priority should be those barriers which discriminate against imports from Third World countries. If these countries were given freer access to western markets, it is they who would have the greatest potential for economic growth and, consequently, for providing import markets for western capital- and knowledge-intensive goods and services.

Although, as we noted above, the growing strength of the service sector and the scientific, engineering, financial, and other expertise that has developed in the industrialized world are highly marketable factors, especially in the Third World, international trade in services remains subject to very widespread national barriers. Yet neither the OECD, which has two codes for liberalizing trade in invisibles between its members, nor GATT have been able to make much headway in bringing down the barriers that affect such important service industries as banking, insurance, shipping, and telecommunications. These sectors involve institutions that are an integral part of, and sensitive to concerns about, national identity and national standards. Canada, for instance, is not about to allow foreign banks to compete equally with its own chartered banks within its borders. So it is with other countries generally. Nevertheless, Canada should take a lead within GATT and the OECD, by giving encouragement to study groups looking at ways to reduce protectionism in services.

The GATT discussions on nontariff barriers, which will, to some extent, take negotiators inside the economic decision-making processes of member countries, may raise the whole issue of the legitimacy of "industrial policy" – a generic term covering all kinds of governmental interventions designed to affect the structure of industry. There are considerable ideological differences on this subject, turning on such questions as "picking the winners," "aiding the adjustment of workers and firms out of unviable industries," and "letting the market decide." In some European countries, industrial policy is seen as a crucial part of building a just and equitable society; in Japan, it has been described as a way of unifying the people in a crusade to maximize the nation's economic potential; in Canada, so far, no consensus is in sight about whether industrial policy is even desirable, although a pot-pourri of government aids to industry has been allowed to develop in the pursuit of various ends. Given these diverse attitudes on the subject, the discussion about industrial policy and nontariff barriers is unlikely to be rapidly concluded.

Other Trading Issues

As a nation that has traditionally relied on its resource base, Canada is sensitive to developments in international commodity markets. Almost inevitably, the volatility of commodity prices has prompted producing nations to try to stabilize prices or earnings from time to time, and OPEC is only one example in the history of cartels and similar arrangements. The depth of the recent recession had the effect of lowering most commodity prices (including energy, metal, and forestry prices), but there are clear signs that recovery is under way – more slowly for energy products than for other commodities. For developing countries, in particular, many of which rely unduly on only one or a few commodities for their foreign-exchange earnings, the instability of prices and markets can prove extraordinarily harmful, rendering their development and industrialization efforts especially vulnerable to cash-flow uncertainties. As more and more nations industrialize their economies, the financial, political, and social problems posed by unstable commodity prices could well become more acute, encouraging even the development of specific trading blocs and barter trade.

The U.S. Department of Commerce estimates that between 10 and 20 per cent of all world trade is done through some form of barter.[14] Eastern European countries have long conducted trade in this way, as witnessed by the terms under which the financing for the gas pipeline from Siberia to western Europe was arranged and by the arrangements by which Rumania recently agreed to purchase a CANDU nuclear reactor from Canada. But the developing countries, too, have seen advantages to barter arrangements; GATT researchers estimate that 40 per cent of the "South-South" trade is conducted on a commodity-swapping basis. Also, within the private sector multinationals have increasingly encouraged their subsidiaries to purchase or barter among themselves before turning to competitors on the open market.

Equally challenging, on the trade front, are the problems posed by the application of economic sanctions and domestic procurement policies. The former follow from the tendency of some of the major nations to use trade as a means of pursuing political or strategic ends. Indeed, sanctions and trade embargoes have become a leading weapon in the foreign policy of the United States – ranging in geopolitical application from eastern Europe to South Africa, the Middle East, and Central America – and there has been a growing inclination to implement them through U.S. subsidiaries incorporated elsewhere, even when the local government objects. The United States is not, of course, alone in imposing sanctions directly or indirectly; it is merely the most prominent user of this weapon.

International Financial Issues

The growing interdependence of world trading activity is reflected in recent developments in other areas of international economic relations. Of particular concern here are the foreign debts of a number of developing and eastern European countries, exchange-rate and foreign-currency-balance issues, and the relationship between trade and investment.

The Foreign-Debt Crisis

Efforts have been undertaken recently to reschedule the foreign debt of a number of major developing and eastern European nations. Large imbalances had emerged in their international payment obligations, primarily as a result of the increase in oil prices and the general sluggishness of growth among western nations, topped off by the recent recession. Overambitious development programs in some countries, sometimes accompanied by heightened social tensions, had aggravated these imbalances. The way in which the foreign-debt problem is handled affects Canadians because it determines the extent to which these developing countries will be able to generate effective demand for Canada's exports. Moreover, international banking consortia – in which a number of Canadian banks have played an important role – are likely to be more careful in the future in financing so much of the economic activity and trade of the emerging nations.

The initial quadrupling of oil prices in late 1973 had raised fears of a shortage of international liquidity, because the oil-exporting countries would be unable to expand domestic demand in line with their oil revenues. These fears proved unfounded: the OPEC members' financial assets were easily recycled, largely through the intermediation of international banks, which in turn responded flexibly to meet the payment imbalances of the oil-importing countries. But rising unemployment in the western economies, combined with increased protectionism, visibly hurt the export prospects of many of the developing countries. Some, such as Mexico and Venezuela, had taken advantage of higher oil receipts to embark on domestic programs of industrial expansion and development of the social infrastructure, with much of this activity being financed through commercial bank loans. The outstanding medium- and long-term debt of the developing countries amounted to over $275 billion (U.S.) in 1978 (Table 2-3) – a sum equivalent to more than 20 per cent of their national income and to the total value of their exports. Eastern European countries also developed large balance-of-payments deficits on imports of foodstuffs, technology, and equipment from the western countries. Thus, when the second increase in the price of oil occurred in 1979, both groups of countries were already experiencing difficulties, and the problems of adjustment took on new urgency.

Table 2-3

Debt Position of the Least-Developed Countries, 1973, 1978, and 1982[1]

	1973	1978	1982
		(U.S. $ billions)	
Total debt	96.8	276.4	505.2
		(Per cent)	
Total debt as a proportion of exports of goods and services	89	111	111
Debt-servicing costs as a proportion of exports of goods and services	14	17	23

[1] At 31 December.

SOURCE L. Dini, "Financial Strains in the World Economy," *Banca Nazionale del Lavoro Quarterly*, 1983.

Much of the accumulated debt was at variable rates and denominated in U.S. dollars. As a result, when the U.S. government opted for a stringent monetary policy in 1981 in order to curb inflation, the extraordinarily high interest rates and appreciated dollar that followed escalated debt-servicing costs; for some countries, the burden became unsustainable. By 1982 the total medium- and long-term debt of the developing countries alone was estimated to exceed $500 billion (U.S.).

In the course of these developments, the international operations of banks expanded at average annual rates of over 25 per cent – faster than nominal GDP or the value of foreign trade. An attraction for many banks, in addition to the profitability of these transactions, was that they led to changes in the structure of world wealth and to an increase in financial intermediation. In addition, they were relatively free of the administrative constraints in force within national boundaries or of the discipline that is traditionally exercised by central banks.

A feature of international banking arrangements has been the development of "rollover" syndicated loans, with a small number of large banks playing a prominent role as "lead" managers on the lending side. Smaller banks participate by buying shares of the loans from the major banks, thereby spreading the risk. This system creates an illusion of freedom from risk that is not warranted, however. Thus in the 1970s the major banks, wishing to preserve preferred relationships with borrowers, particularly governments, tended to underestimate the risks inherent in the individual projects financed by their loans. The small banks, on the other hand, based their assessments of risk on the solidity of the major banks rather than that of the original borrower. Indeed, during the recent debt-rescheduling negotiations, many banks were apparently surprised to learn of the financial liabilities of the borrowing countries, as well as of the numbers of lenders and of the amounts involved. In some cases, too, the major banks appear to have acted on the presumption that their central banks or their governments would intervene on their behalf in the event of trouble.

Canadian banks participated in this process. The international operations of the five largest chartered banks were a major source of profits, particularly in the Eurodollar market. While interest-rate spreads were thin in European loan syndicates, the massive loan sizes produced exceptional economies of scale and lucrative management fees. After 1981, however, most of the banks tended to shift their attention to the U.S. market. Now that Canadian banks have tended to draw back from syndicated international lending, the rate of growth of their foreign assets is expected to slow down over the next few years.

On the broader front, it is clear that the foreign-debt problem of the developing countries will persist for some time, although lower U.S. interest rates and a reduction in the exchange rate of the U.S. dollar would help significantly to lessen that burden. The rapid growth of bank lending to these countries was partly a consequence of the inability of official financial and foreign direct investment to keep pace with their financing requirements. Now, with a slowdown in bank lending, it is essential either that there be more official and long-term financing available or that there be sufficiently healthy growth in their exports to enable them to cover their debt-servicing needs. Economic growth in Latin America, for example, has stagnated after having averaged close to 6 per cent annually throughout the 1970s. Renewed growth there and in other developing countries depends critically on the vigour of the economic expansion in the OECD area. The extent is revealed by simulations of world economic conditions, which show that only under a quite optimistic expectation of OECD recovery and expansion – i.e., an average annual growth rate of at least 3 per cent to the end of the century – could the developing countries expect to regain the kind of manageable debt/export ratios that were achieved in the 1960s.[15] A slower growth rate for the OECD – averaging, say, 2 per cent annually – and less advantageous terms-of-trade developments would leave the major borrowers among the least developed countries in the same precarious situation that they are now experiencing.

From Canada's perspective, therefore, it is not enough to assume that renewed OECD growth and expanding trade will, if accompanied by domestic adjustment policies within the borrowing countries, reduce the current world debt situation to a fairly short-term liquidity issue. For many countries, part of the solution may lie in developing a more favorable climate for direct foreign investment. Some will also require austerity programs in order to restore lender confidence and to provide incentives for banks to commit new funds. The danger of austerity programs is that, if they are imposed with great severity, they could well create the kinds of political and social strains that would jeopardize domestic economic growth; indeed, some countries have already experienced such difficulties. Choking off new loans presents the risk of precipitating new crises and, in effect, turning good debt into bad.

From the point of view of the international banks, including those Canadian banks that are exposed to the international debt problem, the adjustments are risky and costly. The extreme risk – which does not now seem very likely – is that one or more of the international debts will not be met or rescheduled satisfactorily and that large loan losses may jeopardize the solvency of the banks themselves. For some banks, including some Canadian ones, the possible exposure to bad external loans, in combination with large domestic writeoffs, is substantial. While the central banking systems of Canada and most other developed countries have a large capacity to provide safety nets or underpinnings for their commercial banks, this contingency would give a serious jolt to the international financial system.

Even if the extreme risk does not arise, there are other costs. If interest payments on the debts are delayed or reduced, the current earnings of the banks will also be reduced. The amounts of the debts that must be rescheduled are large, and further loans may be necessary for some debtor nations to meet interest payments to accommodating creditors. Moreover, the incidence of these external-debt problems, coinciding with recession-hit loan portfolios domestically, has prompted many of these banks to adopt more cautious lending policies, with a dampening effect on the economic recovery in some countries. To a degree, this has been a factor in Canada.

The provision (by the Schedule A banks) of reserves for loan losses of close to $450 million in the first quarter of 1983 was more than 60 per cent larger than the $275 million provision set aside in the first quarter of 1982. It has been suggested that if the banks are to escape being burdened by these debt-adjustment problems for some years to come, the governments of the richer countries may have to help them to meet their liabilities, directly or through international organizations.

The strategy for dealing with the international debt situation that was discussed and endorsed by the leaders of the major industrial nations at the Williamsburg Summit earlier this year involved a careful balance between offers of financing facilities and the encouragement of domestic austerity and adjustment to meet the standards of the International Monetary Fund (IMF). It was recognized that involvement by both the IMF and the World Bank is necessary, along with that of the newly created private Institute of International Finance, to develop a system of exchange of information on foreign-loan exposures that will help lenders to assess more accurately the project risks in the borrowing countries. At the same time, it is widely recognized that the role of the IMF must be enhanced if it is to provide borrowing countries with more regular guidance on appropriate debt levels and on policies that will enhance domestic restraint and export promotion. This will involve a substantial increase in IMF quotas and an enrichment of its General Arrangements for Borrowing. It could also involve a major expansion in the funding of the World Bank, so as to induce new flows of bank credit to the developing countries in concert with expanded World Bank activity. Clearly, there is a need to clarify and strengthen institutional arrangements aimed at encouraging and protecting foreign investment and direct aid, while expanding trade opportunities. Part of the strategy for gradually reducing the debt/export ratios of the developing countries and eastern Europe should, therefore, involve IMF and World Bank activity, in combination with OECD initiatives that would open markets and provide for relatively noninflationary growth, and with measures by the developing countries themselves to follow prudent economic policies in their own right.

Currency Developments

Among the more striking developments in the early 1980s has been the steep rise of the U.S. dollar in exchange markets vis-à-vis most European currencies. From its low in late 1978, the U.S. dollar has increased by over 30 per cent against the West German mark and the Japanese yen; and with it the Canadian dollar too has appreciated, although less notably. There have been substantial differences in the monetary policies and fiscal stances adopted by the major western nations, with variations in interest rates among countries that have ranged as high as 10 percentage points and are currently in the 5-point range. Such shifts in currency values, coupled with the increasing participation of banks in international lending and financial intermediation, have put strains on the economic strategies and financial management of OECD member countries, balanced as they must be by domestic concerns over the recession and the extraordinarily high levels of unemployment throughout Europe and North America.

The expansion of international trade has been accompanied by large increases in the foreign-currency balances held by private financial institutions, nonfinancial corporations, and individuals. In Canada, the relatively small but strong reserve position required of chartered banks has allowed for new and highly sophisticated kinds of financial management, so as to provide maximum earnings leverage. Many institutions have been willing to pay premiums for standby credit in order to enter into contractual arrangements with foreign borrowers, and billions of dollars of capital flows change hands daily. For instance, the foreign-currency liabilities booked in Canada by Canadian residents (i.e., their holdings of financial assets in foreign currencies, especially U.S. dollars) increased from $2 billion in 1974 to $16 billion in 1980 – a compound growth rate of 37 per cent annually. During the same period, Canada's official international reserves diminished from slightly under $6 billion to $4 billion (a decline of 6 per cent annually), with the result that private holdings of foreign currencies were four times the size of Canada's international reserves in 1980, whereas they were only 40 per cent higher in 1974. This development, which is not confined to Canada alone, reflects a long-term change that could have a bearing on private- and public-sector decisions about exports, imports, capital flows, and cash management. It probably means that, during the 1980s, there will be greater volatility of exchange rates and greater pressures for Canadian producers, importers, and exporters to adopt new accounting rules, use currency options, and seek tax charges in order to adjust competitively.

Investment

Another field of interest is the interaction between trade and investment since, as we observed earlier, direct investment in production facilities abroad is increasingly becoming a part of the international logistics of very large corporations with branch plants in many nations. While intracorporate links are characteristic of North American trade, they are less prevalent worldwide – one estimate suggests that 15

Table 2-4

Flows of Direct Investment Capital Between Canada and All Countries and Between Canada and the United States, 1974-82

	Foreign investment in Canada		Canadian investment abroad[1]	
	All countries	United States	All countries	United States
		($ Millions)		
1974	+845	+684	-810	-524
1975	+725	+588	-915	-542
1976	-300	-559	-590	-257
1977	+475	+417	-740	-508
1978	+85	-300	-2,150	-985
1979	+675	+328	-2,500	-1,210
1980	+585	+118	-3,150	-2,216
1981	-4,600	-3,565	-5,900	-3,110
1982	-1,425	-2,281	+200	+742

[1] A minus sign indicates a positive net outflow from Canada; a plus sign, a reverse net flow into Canada.

SOURCE Statistics Canada, *Quarterly Estimates of the Canadian Balance of International Payments*, Cat. 67-001, first quarter 1983, pp. 64-5.

to 25 per cent of the manufactured-goods trade is between affiliates[16] – but it is spreading. These transactions introduce complex subtleties into a trading situation that is vastly different from that which existed in the late 1940s and the 1950s, when GATT and other instruments of international negotiation and surveillance were first put into place.

Of prime consideration for Canadians are this country's traditional reliance on high levels of gross fixed-capital formation and worries over excessive foreign ownership or control. Insofar as direct investment is concerned, however, for some time now there has been a net outflow of equity capital from Canada. Increasing Canadian takeovers of U.S. companies, along with real estate and other ventures in the United States, have given rise to heavy flows of direct investment funds abroad throughout most of the period from 1978 on, while within Canada there have been major purchases of foreign-owned assets by Canadians, mainly in response to the provisions of the National Energy Program. In 1981 alone, the Canadianization of foreign-owned assets, plus the direct investments made by Canadians in other countries, produced a combined outflow of over $10 billion and direct upward pressure on Canadian interest rates. These outflows subsided in 1982 and the first half of 1983, as concern over corporate balance sheets in Canada prompted a more prudent approach to foreign acquisitions. The volatility of these flows is apparent from Table 2-4.

On the other hand, the net issues of bonds to nonresidents, which had been falling in the late 1970s, jumped to over $10 billion in 1981 and $12 billion in 1982. Prominent here were the issues of provincial governments hit by budgetary deficits, as well as those of provincial crown corporations. The federal government and its enterprises were also active borrowers, mostly in the European market, where the high interest-rate differentials made Canadian securities an attractive investment.

Possible Fresh Initiatives

A sophisticated debate is ensuing, addressed to the question of whether GATT's hitherto inviolate principle of "nondiscrimination" in trade bargaining – the rule that any concession made by a country in negotiations with another must apply multilaterally – ought to be amended or qualified in some fashion. Until now, this has been debated only among trade specialists, but the idea may gain wider currency if the world economic recovery gathers strength and the unemployment problem proves less intractable than is forecast at present. This issue may involve Canada directly if the suggestions that have been put forward in some quarters for selected sectoral U.S.-Canada free-trade arrangements are pursued. While such arrangements are not necessarily out of spirit with the GATT principles if they are developed in the context of reduced North American tariff barriers, they clearly would be of a bilateral, preferential nature and could be construed as discriminatory against other trading nations.

Another issue preoccupying GATT participants is the method of "graduation" to be used to move newly thriving Third World countries, whose exports have been receiving special preferential one-way tariff treatment in advanced nations, to the normal status of GATT members obtaining no more privileged access in other markets than they themselves afford foreign goods in their own. Countries such as South Korea have reached a stage of industrial success and a level of national wealth at which the advantages provided to Third World states under the GATT's Generalized System of Preferences (GSP) no longer seem to be justified. The trouble is that the countries concerned naturally do not wish to give up a benefit and obtain nothing in return. Because each developed nation has its own "generalized preference tariff" structure under the GSP arrangements, any country seeking to withdraw that privilege from a particular trading partner might find that partner so aggrieved as to retaliate in some way. Clearly, the graduation process should be tackled internationally and carried out in a manner that would yield positive longer-run consequences for the countries that, after all, have escaped out of material poverty and propelled themselves into the ranks of developed and prospering societies.

In the current international reassessment of trade policy, considerable emphasis is also being placed on the problem of restrictions against commerce in agricultural products. This is a subject of controversy mainly between the United States and the European Economic Community. It focuses on the EEC's "common agricultural policy," a carefully structured system of farm-price supports, import levies, and other devices designed to maintain agriculture as a healthy feature of the European economic and social scene. The United States has expressed considerable dismay at alleged EEC overproduction and dumping of agricultural commodities in third markets, as well as at the GATT treatment of agricultural trade issues. It is joined by Canada and Australia in these perceptions. But the CAP is viewed in Europe as an element of social policy, and indeed as a means of sustaining a key aspect of European tradition. The increasingly vigorous attempts by the U.S. delegation at Geneva to force a change on the part of the Community in this respect have met with little success.

Moreover, although the principal battleground on the farm trade issue is in Europe, agricultural policies in Japan and in other important potential markets (like South Korea and Taiwan) are, in many respects, equally protectionist and for approximately the same reasons. While the chances of a major shift in agricultural support arrangements in any of these countries are relatively slim in the medium term, the logic of comparative advantage may gradually convince governments in western Europe and the Far East that some reform of their systems is called for. It remains to be seen whether the United States' aggressive approach to the problem will be more effective than the softer tone adopted by Canada.

Two relatively new initiatives on the agenda of international trade negotiations, both sponsored by the United States, are concerned with lowering the barriers against the exchange of services and against commerce in high-technology goods. Fundamentally, the U.S. position is that these are sectors of strong growth and competitive advantage in the future for countries at the leading edge of economic development.

We have already discussed the trade in services and the prospect of its growing importance for those economies which have reached the postindustrial phase of evolution. Evidently, there are worries that the potential for fully exploiting the opportunities in this sphere could be thwarted by obstacles introduced by less advanced nations, fearful that the gains would accrue principally to the advanced industrial countries at the expense of their own perceived national interest. Reluctance to deal with this topic was immediately expressed by Third World nations when it was introduced at the GATT ministerial meeting last year, and they finally agreed only to a program of studies by signatory countries, aimed at accumulating more facts and figures on the subject.

The discussions about trade in high-technology products are often characterized more by trendy jargon than by clear substance. Here again, however, there is nervousness lest "national interest" considerations cause countries to create barriers or otherwise interfere in a field where the most advanced industrial nations have a strong edge. Nevertheless, it is not entirely clear why high-technology products should be placed in a special category in trade strategy, since the goods involved are essentially similar to any others entering the international marketplace.

A New Era for Trade Negotiations

What do the developments described above imply for Canada in the medium term? First, while this country's export strength has traditionally been based on its mineral, agricultural, and forestry endowments, world trade over the next decade will likely tilt away from primary products. Second, Canadian manufacturers can look forward to significantly stiffer competition; increasingly, the concept of comparative advantage is viewed as ephemeral, based less on fixed resources and more on scientific knowledge and human ingenuity that, in the global context, can be applied in many alternative locations. To remain viable in the world economy, Canadian manufacturers must be alert to new technological developments and to the importance of good labour relations in improving productivity performance. Third, while tariff barriers remain an important deterrent to Canadian manufacturing efficiency, they are becoming less so. More serious are the host of nontariff barriers that are being adopted and the uncertainties associated with international lending and volatile exchange rates. Fourth, services are likely to be an area of growing trade opportunity where, despite many serious national barriers, Canada should be adept in developing expertise and effective marketing practices. Finally, although Canada's place in the North American market remains secure, the recent period of slow growth and recession has hit Canadian trade with western Europe. While the United States and the other OECD nations will continue to command the lion's share of Canada's trade in the medium term, the newly industrializing and emergent nations are expected to achieve the highest growth rates in incomes and in international trade. One hopes that this will provide ample scope for additional Canadian trade, but the Canadian manufacturing and service firms that will benefit are not likely to be those in the low-skilled category.

In *The Bottom Line*, the brunt of evidence, though not completely clear-cut, was that lowering trade barriers does yield higher productivity, larger plant sizes, longer production runs, and lessened product diversity.[17] There is a natural turnover of firms within industries, and the adjustment costs for businesses are not excessive. Labour adjustment problems, while frequently acute for the persons involved, are capable of resolution in an expanding economy, provided that there is adequate prior consultation, as well as sensitive retraining and income-support programs in place to ease the process of change. That being said, high levels of unemployment now and in the future will make the adjustment process more difficult, particularly where it involves older persons with a substantial number of years of service.

This Council remains as committed as ever to the concept of freer trade as an instrument to further prosperity and as a part of the almost inevitable process of global integration. In its trade no less than in its international financial transactions, Canada as a medium-sized nation has a need for outward-looking measures. That this entails many uncertainties – exchange-rate volatility, loan reschedulings, defaults, and the like – there can be little doubt, but the rewards would seem to outweigh by far whatever additional risk premiums must be paid.

3 Recession and Recovery

The recent economic news has been encouraging for Canadians. After six quarters of negative real growth, the economy has begun to move forward again; the rate of inflation has fallen to single-digit levels; interest rates have dropped substantially from their previous peaks; and the housing industry is in the midst of a substantial recovery. The April 1983 budget of the federal government announced a recovery program that has increased the level of confidence of the business community, removing many uncertainties in the fiscal area that had lingered for a few years. Monetary policy has evolved as supportive but cautious, with the Bank of Canada determined to avoid credit policies that could unbalance the recovery on either the up side or the down side.

Despite all this good news, there remain areas of concern. Close to 1.5 million Canadians are still without jobs. The impact of the recession on the tax base and expenditures of the federal government, including its spending under the Special Recovery Program announced in the budget, has put upward pressure on its deficit, leaving unanswered a number of questions pertaining to the characteristics of the gap between revenues and expenditures. For example, is the federal deficit related only to the deep cyclical trough that was experienced during the early 1980s? Does it comprise other components? There is some evidence to suggest that part of the current deficit at the federal level in the United States is structural. What is the evidence for Canada?

During the next year or so, we expect a substantial improvement in the level of real GNP, some reduction in the unemployment rate, continued moderation in the rate of price increases, some improvement in productivity performance, and only slight deterioration in the federal deficit. But what about the medium term? Will the recovery lead to a period of sustained growth for Canada? Will there be a further decline in the unemployment rate? A return to long-run price stability? A resurgence of capital investment? A reduction in the borrowing requirements of the federal government? The emergence of a strong competitive position for Canada in world markets?

The durability of the current economic recovery in Canada – or, for that matter, in North America as a whole – is a matter of concern. There have been two economic contractions since 1972. The recovery that followed the first of these was not solidly based, however, as shown by the damaging role that the second oil price shock and its effect on price expectations played during the late 1970s and early 1980s, leading to the implementation of tight credit conditions in North America and a severe downturn in economic activity.

During the current recovery period it would be easy to focus on the short-run results that are favourable and to ignore many of the problems that have plagued Canada since the mid-1970s. That would be counterproductive, however, as there are important lessons to be drawn from the recent recession, and difficulties that must be resolved. Among other things, the impact that the federal deficit could have on financial markets in the medium run must be assessed; and the problem of unemployment, which remains the most visible scar of this past period of poor performance, must be tackled.

The Recession Abroad

The second oil price shock in 1978-79 was accompanied by a nearly unanimous swing towards restraint in the monetary and fiscal policies of the OECD countries. During this period both the monetarist and supply-side viewpoints prevailed, and policies designed to contain the inflation that arose from the shock were implemented. The combination of a tight monetary policy, resulting in high nominal and real interest rates, and generally restrictive fiscal policies in many countries curtailed real economic activity more than anticipated. In several cases, the effects of tight fiscal policy were not as apparent as those of monetary restraint. A cursory examination of the deficits might suggest the opposite, however. For example, debt-servicing costs, influenced by high nominal interest rates, exerted upward pressure on deficits. In addition, the automatic stabilizers – i.e., reduced tax revenues and increased social security payments during cyclical downturns – combined to offset deliberate restraint in government expenditures.

Real growth in the OECD countries declined by more than 1 per cent in the first half of 1982; this was followed by a weak recovery during the second half of the year (Table 3-1). There was reduced trade with countries outside the OECD area because of the effects of the recession on non-oil developing countries, with the savings from lower energy costs being mitigated somewhat by the appreciation of the U.S. dollar – the currency in which OPEC prices are set. This was accompanied by declining energy revenues in the OPEC countries, which curtailed their imports from the OECD area as a result.

Table 3-1

Real Growth in OECD Countries,[1] 1981-83

	All OECD countries	Seven major countries[2]
	(Per cent)	
1981 – First half	2.4	2.9
– Second half	0.3	0.1
1982 – First half	-1.0	-1.2
– Second half	0.6	0.6
1983 – First half[3]	1.7	2.0
– Second half[3]	3.5	4.0

[1] Seasonally adjusted annual rates of change over preceding period, calculated with 1981 prices and 1981 exchange rates.

[2] United States, Japan, West Germany, France, the United Kingdom, Italy, and Canada.

[3] OECD forecasts.

SOURCE OECD, *Economic Outlook*, July 1983 and previous issues.

The recession, together with the subsequent weakening of world oil prices, produced a dramatic slowdown of inflation; this was, however, offset by a rise in unemployment in most countries. The recession also encouraged a variety of protectionist arguments, some of which were reinforced by large deviations in exchange rates from the levels consistent with underlying cost and price conditions. In addition, the interaction of falling commodity prices and depressed levels of trade intensified the strained financial plight of many developing countries. Deteriorating external balances and growing debt obligations, accompanied by high interest rates, contributed to difficult conditions in several countries – Brazil, Mexico, and Argentina, among others.

For the OECD area as a whole, it now seems that the worst is over. In the first half of 1983 the United States led the recovery in demand and output, with many of the other member countries contributing to some degree. An easing of U.S. monetary policy, lower interest rates, lower oil prices, and an increased level of consumer confidence were among the factors of the recovery. Trade, however, remains somewhat hampered.

In most OECD countries, unless new, and as yet unannounced, initiatives are taken in either the public or the private sector, the recovery will not be strong enough to have a substantial impact on labour markets. The OECD labour markets are expected to remain weak, with unemployment rising in most European countries, particularly among the younger groups of workers. Modest reductions in unemployment rates in North America, like those which occurred in the early part of 1983, will not be enough to counteract these pressures. As a result, global conditions will cause overall OECD unemployment rates to stabilize at high and unsatisfactory levels. Furthermore, the improvement that has occurred on the inflation front could be short-lived as the recovery exerts pressure on non-oil commodity prices, many of which have fallen drastically over the past two years. Increased energy demand, resulting from the acceleration of economic activity, could also bring about a firming and subsequent rise of international oil prices in excess of general inflation rates by the mid-1980s. Yet if, in order to contain inflation, tighter monetary measures were adopted in the United States, leading to higher interest rates, the whole recovery process could falter.

In the major OECD countries, the intensity of the recession depended on domestic policy response and on the degree of participation in the international economy (Tables A-2 to A-6). In *Japan*, performance remained better than in the other countries, although it was substantially lower than it had been previously. Japanese real growth remained in a range between 3 and 4 per cent, as active demand-management policies, supplemented by sectoral intervention, permitted the pursuit of monetary and fiscal policies that were designed to influence domestic demand and to control inflation. Thus, despite a somewhat severe contraction in export demand resulting from shrinking world markets and from bilateral agreements limiting exports to various markets (such as those concerning Canadian and U.S. automobiles), consumption and investment remained strong. Inflation in Japan declined from about 5 per cent in 1981 to between 2 and 2.5 per cent. At the same time, even though Japanese unemployment rates were among the lowest of all OECD countries, there was some upward pressure towards the end of the period. Although declining trade volumes have influenced Japan's normally robust trade surplus with its OECD trading partners, the appreciation of the U.S. dollar during the period and the concomitant depreciation of the yen have intensified competition and exerted pressure on external balances within the OECD area.

In western Europe, the intensity of the recession was less severe than in North America but more so than in Japan. In *France*, government policy reluctantly shifted away from its earlier emphasis on job creation towards a more restrictive fiscal policy. Real GNP growth gradually recovered to a range between 1 and 2 per cent, with considerable strength in consumer spending during much of the period, although that strength is now weakening as new taxes cut into real incomes. Inflation peaked towards the end of 1981 at over 14 per cent; while it has now declined to about 9 per cent, it is still on the high side with respect to the overall OECD experience. At the same time, government policies adopted at an early date to contain, if not reduce, unemployment meant that French jobless rates did not experience the severe upward pressures common to the majority of the other OECD countries. The marked deterioration of the government budget balance and of the external trade balance, along with the accompanying pressures of devaluation in 1982 and a further realignment of the franc in 1983, has acted as a serious constraint on government policy formulation.

Throughout most of the 1970s *West Germany* was quite successful in combining relatively strong growth with low rates of inflation and unemployment. But in the most recent recession, unlike France, West Germany suffered from weak consumer demand, as unemployment rose and real incomes deteriorated. A restrictive public stance, coupled with high nominal interest rates, acted as a disincentive to recovery. Real growth performance was dismal, with negative rates being recorded for most of the quarters under review. For much of the period, export activity was the major source of strength, but that, too, was hampered as import spending by the OPEC countries and others faltered under the weight of the recession. Despite a reduction in the number of migrant workers, the jobless rate almost doubled, becoming particularly high among the young. Fiscal pressures on the government resulted in the deficit remaining close to [illegible] per cent of GNP throughout the period. The external position has remained reasonably viable, as declining export revenues have been offset by reduced import spending, including a lower oil bill.

Cyclical fluctuations in *Italy* were more severe than in many other OECD countries, with serious imbalances emerging in the economy. Weakening export competitiveness and restrictive monetary and fiscal policies that inhibited domestic demand (including a considerable reduction in investment activity) combined to produce a sluggish economy, with serious deterioration occurring over the second half of 1982. While the inflation rate has declined from over 20 per cent to about 16 per cent, unresolved wage pressures exerted by various forces, such as a program of universal wage protection (the *scala mobile*), have inhibited further reductions. While these and other pressures nudged the unemployment rate close to the double-digit threshold, the results in Italy have not been as severe as in other OECD countries. Retention of a healthy tourist economy has helped to keep the Italian current account close to balance. Recessionary pressures, however, have contributed to a government deficit that approached 12 per cent of GDP during the period.

By the end of 1982 real growth in the *United Kingdom* had recovered from the negative rates of 1981 to exhibit considerable strength relative to that of Britain's trading partners. This strength has emerged in both consumption, as the result of an improvement in real incomes, and investment, because of ongoing energy activity. Inflation declined dramatically from over 12 per cent in the first quarter of 1981 to less than half that figure two years later. This improved performance has not been matched by employment growth, however; as a result, unemployment rates have remained at double-digit levels and are gradually rising, with severe dislocations occurring among the young. The consequent increase in social security benefits has strained government balances, although this has been offset by the North Sea oil revenues accruing from increased exports to many countries. As a result, Britain's current account balance has remained in surplus throughout the period. Generally, although serious problems remain, the British economy is now seen as much stronger than it was after the initial OPEC shock.

In 1981-82 the *United States* implemented a very tight monetary policy that resulted in exceptionally high nominal and real interest rates and eventually had a major deflationary effect. The trough of the U.S. recession was reached in the third quarter of 1982, with a gradual upturn beginning at the end of that year. Inflation rates have fallen dramatically in the United States, assisted by moderate wage settlements, declining energy and commodity prices, and the appreciation of the dollar. While unemployment rates remain high, they are declining. As far as the budget is concerned, recessionary pressures and defence spending, as well as the tax measures already implemented by the Reagan Administration and the tax package that it has introduced for 1983-84, have combined to bring the government deficit to close to 4 per cent of GNP. Since its appreciation in 1980, the strength of the U.S. dollar has contributed to a gradual deterioration in competitiveness and some pressure on external balances. Naturally, developments in the U.S. economy have had, and will continue to have, a major impact on the Canadian economy.

The Recession in Canada

It is useful to look more closely at how the recession has altered the Canadian economy, with particular reference to four areas: unemployment, inflation, government balances, and the external balance.

The Effect on Unemployment

Unemployment is Canada's major problem: the jobless rate rose from an average of 7.4 per cent in the first quarter of 1981 to a peak of 12.7 per cent in the fourth quarter of 1982 (Table 3-2).[1] It now stands at 12 per cent, with the rate for men exceeding that for women. The high rate of unemployment among young men (aged 15 to 24) explains this phenomemon in part. Employment in this group fell by 272,000 between January 1981 and December 1982, while its unemployment rate rose from 13.5 to 24.0 per cent. The severity of the situation is even more evident if one considers that the participation rate of young men declined even as their unemployment rate increased. The situation for young women was also gloomy, though not as severe. Of equal concern, however, has been the increase in the number of jobless in the "primary" labour force (men aged 25 to 54). In January 1981 the rate for this group was 4.5 per cent, but by December 1982 it had risen to 10.2 per cent. This increase reflected the severity of the recession in the goods-producing sectors, particularly manufacturing and construction, which more recently have shown some modest recovery, however.

Regionally, the traditional areas of high unemployment (Newfoundland, Nova Scotia, New Brunswick, and Quebec) were severely hit. One out of every five labour force participants in Newfoundland was unemployed; in many communities, the ratio was even higher. Other areas that had experienced low levels of unemployment in previous years have also been hit. Alberta's unemployment rate, which was 3.6 per cent in January 1981, had risen to 10.6 per cent by December 1982. Although factors other than the recession contributed to the Alberta situation, what was once a bright employment picture has now severely deteriorated.

The impact of the recent recession on the labour market, compared with that of earlier slowdowns, can be measured by breaking down the variations in per capita output into "intensity" of labour application, as measured by hourly productivity and hours worked per employee, and "quantity" of labour application, as measured by employment and participation rates at the individual level (Table 3-3). In 1982 the

Table 3-2

Selected Economic Indicators, Canada, 1981-83 (Quarterly Figures)

	1981				1982				1983
	I	II	III	IV	I	II	III	IV	I
					(Per cent)				
Unemployment rate[1]	7.4	7.2	7.4	8.4	8.9	10.5	12.1	12.7	12.5
Year-over-year change in consumer price index	12.2	12.6	12.7	12.3	11.5	11.5	10.6	9.7	7.6
Current account balance as a proportion of GNP	-1.1	-1.9	-3.1	-0.8	-0.1	1.1	1.3	1.2	0.2
Federal balance as a proportion of GNP[2]	-1.6	-1.7	-1.9	-2.9	-4.2	-5.3	-7.3	-6.5	-6.7
Provincial balance as a proportion of GNP[2]	0.1	-0.3	-0.2	0.2	-0.1	-0.9	0.5	-1.7	-0.6

1 Seasonally adjusted quarterly averages.
2 Seasonally adjusted at annual rates.
SOURCE *Bank of Canada Review*, May 1983; and Statistics Canada, *National Income and Expenditure Accounts*, first quarter 1983.

Table 3-3

The Effects of Recent Recessions on Selected Labour Factors, Canada, 1975, 1980, and 1982

	1975	1980	1982
		(Per cent)	
Change over previous year in:			
Per capita output[1]	-1.7	-1.0	-6.2
Hourly productivity[2]	--	-1.1	-1.6
Hours worked per employee[3]	-0.7	-0.8	-0.2
Rate of employment[4]	-1.7	--	-3.7
Participation rate[5]	0.7	1.0	-0.9

1 Gross domestic product at constant prices/population aged 14 and over.
2 GDP at constant prices/person-hours worked.
3 Person-hours worked/number of employed.
4 Number of employed/labour force.
5 Labour force/population aged 14 and over.
SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

declines in output and productivity were substantial, and the decrease in hours worked per employee was fairly small, compared with the figures for 1980 or 1975.

Almost 90 per cent of all job losses from 1981 to 1982 occurred in the goods-producing industries (Table 3-4). The recession prompted many firms to cut costs and improve staff flexibility by maintaining, or even increasing, the number of part-time employees. Whereas the number of full-time employees in this sector fell by 10.2 per cent between 1981 and 1982, the number of part-time employees increased slightly – by 1.7 per cent. In the service industries, too, the largest increases in part-time personnel occurred in the sectors registering the largest declines in full-time jobs. Much of the part-time work was undertaken by employees who sought, but could not find, full-time work. According to the Labour Force Survey, in 1982 almost one-fourth of those working part-time stated that they had been unsuccessful in finding full-time work.

It is not surprising, then, that men were more adversely affected by job losses than women. An examination of recent trends in the demographic structure of unemployment shows that a break occurred in the fourth quarter of 1981, as massive layoffs began in the goods-producing industries, primarily affecting men aged 25 and over (Chart 3-1). In the third quarter of 1981 this group accounted for just 29 per cent of all the unemployed; by the end of the following year that figure had climbed to almost 37 per cent. These developments inevitably put pressure on the unemployment insurance system: the number of UI beneficiaries increased 2.4 times between September 1981 and December 1982.

Table 3-4

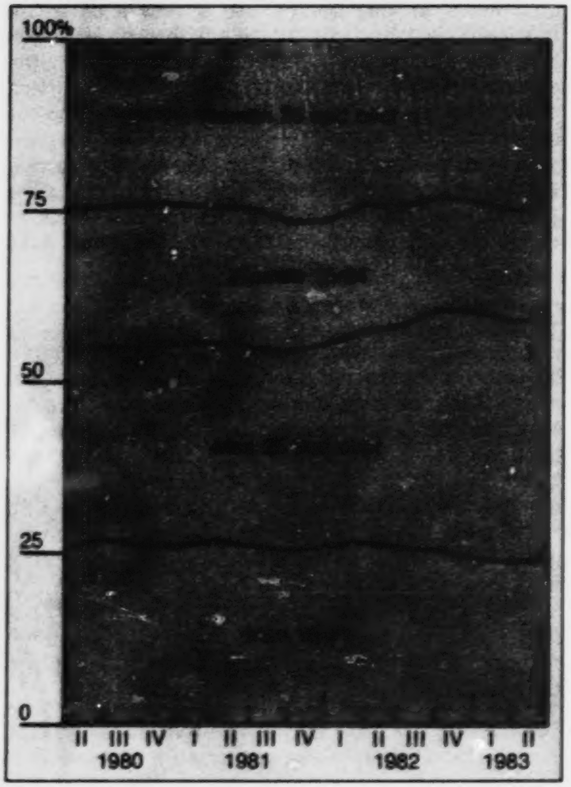
Changes in the Employment Situation, Canada, 1980-82

	Employment in 1980	Variation in employment			
		1981/1980		1982/1981	
	(Thousands)	(Thousands)	(Per cent)	(Thousands)	(Per cent)
Goods-producing industries	3,497	66	1.9	-321	-9.0
Agriculture	477	7	1.5	-19	-3.9
Other primary industries	296	18	6.1	-53	-16.9
Manufacturing industries	2,105	15	0.7	-194	-9.2
Construction	619	26	4.2	-55	-8.5
Service industries	7,158	212	3.0	-39	-0.5
Transportation, communications, and other utilities	901	3	0.3	-29	-3.2
Trade	1,830	45	2.5	-36	-1.9
Finance, insurance, and real estate	608	-16	-2.6	9	1.5
Community, business, and personal services	3,079	159	5.2	17	0.5
Public administration	740	21	2.8	-	-
All industries	10,655	278	2.6	-359	-3.3

SOURCE Statistics Canada, *The Labour Force*, Cat. No. 71-001.

Chart 3-1

Composition of Unemployment by Demographic Group, Canada, 1980-83



SOURCE Statistics Canada, *The Labour Force*, Cat. 71-001.

The Effect on Inflation

The deceleration in the rate of increase of the consumer price index has been dramatic. Averaging 12.5 per cent in 1981, growth in the CPI had fallen to 7.6 per cent by the first quarter of 1983. Many factors have been associated with this reduction in inflationary pressures in Canada. They include: the decline of commodity prices at home and abroad; the reduction in interest rates; the stability of the Canadian dollar against its U.S. counterpart; the impact of slack labour and product markets both in Canada and abroad; and the reduced wage settlements in the public sector through the "6 and 5" program and related provincial restraint programs, and through their demonstration effect on many settlements in the private sector. The weakness in international energy prices has had little effect on Canadian energy prices, however, because of the regulated pricing system in effect in this country.

A look at the path of the components of the CPI over the last nine quarters makes it clear that food prices, which have a 21 per cent weight in the index, have played a major role in slowing down the general rate of inflation. Whereas they had risen by close to 14 per cent in the first quarter of 1981, by the fourth quarter of 1982 this increment had declined to 7 per cent; it dropped still further to 5.4 per cent in the first quarter of 1983. Weak international commodity prices have had a major impact on this component of the CPI – a trend that could reverse in the near term.

Major wage settlements in all industries (excluding construction) fell from an average of 13.3 per cent in 1981 to 10.0 per cent in 1982 and to 6.6 per cent in the first quarter of 1983.[2] The largest decline was in the commercial sector, where wage increases fell from 13.8 per cent in 1981 to 9.5 per cent in 1982 and to 6.1 in the first quarter of 1983. Unit labour costs in the goods-producing sectors have shown a declining trend since the third quarter of 1981, with the reduction being particularly strong in manufacturing. After exchange-rate adjustments, however, Canadian unit labour costs (calculated in U.S. dollars) still increased somewhat more than those in the United States, while, on the same basis, those of our overseas trading partners fell.[3] This could bode ill for Canada's longer-run competitiveness – an issue to which we shall return in the final chapter.

The Effect on Government Balances

The financial position of all levels of government has been made much more difficult by the impact of the recession (see Table 3-2). The federal government's position steadily deteriorated between the first quarter of 1981 and the first quarter of 1983. Several factors have combined to produce this result.

The costs of the social "safety nets," which inevitably grow during a recession, have caused federal expenditures to rise above their long-term trend. For example, federal transfers to persons soared from $18 billion (on a seasonally adjusted basis) in the first quarter of 1981 to $27.7 billion during the first quarter of 1983. A large portion of this increment was due to the increase in unemployment insurance payments. Other components of transfers were affected by the restraint imposed under the "6 and 5" program, however. Higher expenditures have also resulted from the gradual implementation of federal incentive programs, such as the Special Recovery Program. Because of the reduction in interest rates, debt-servicing costs have not been as important an item as they might have been had interest rates remained at their 1981 peak. Nevertheless, these costs constitute a higher proportion of the total budget than in the period prior to the recession.

On the revenue side, the reduction of economic activity has lowered direct tax revenues from both persons and corporations. The weakness in international oil prices has meant that the potential federal revenues expected from the various energy taxes that were implemented after the introduction of the National Energy Program and its subsequent revisions have not been realized. Indirect tax receipts dependent on consumer spending have also been reduced. The net result of all of these factors has been an increase in the federal deficit from 1.6 per cent of GNE in the first quarter of 1981 to well over 6 per cent by the first quarter of 1983.

Provincial governments have been affected just as severely by the recession, although the results vary from province to province and over time. The picture has generally been one of reduced tax revenues, as the result of depressed economic activity and dramatically increased safety-net spending to offset the severe effects of the recession on individuals. In the case of the energy-producing provinces, lower levels of international oil prices and the gloomy investment environment have led to reduced royalty and lease revenues. The overall balance for all the provinces fluctuated between 0.5 and −1.7 per cent of GNE between early 1981 and early 1983. This disguises some especially severe pressures in the provinces where the recession had the most serious impact.

The Effect on the Current Account Balance

Because of the high import content of economic activities in Canada, high levels of economic growth generally imply a reduction in the merchandise trade balance. The extent of the reduction is tempered by the degree of export demand and the movement in the terms of trade. At the same time, the traditional deficit on trade in services remains a fact of life, dominated by the debt-servicing requirements of Canada's external obligations. Thus in good times Canada's current account balance tends towards deficit. Bad times often reverse this pattern, and the recent recession is no exception (see Table 3-2). As the recession deepened over the last three quarters of 1982, the current account balance moved to a surplus position, peaking at 1.3 per cent of GNE in the third quarter. The merchandise trade balance, which had been $7.4 billion in 1981, swelled to $18.3 billion in 1982 – the largest merchandise surplus ever recorded for Canada.

Numerous factors contributed to this situation. The deepening recession reduced Canadian consumption of foreign goods, with merchandise imports falling by nearly $11 billion between 1981 and 1982. While part of this reduction was linked to depressed economic activity, a declining oil bill occasioned by both reduced international prices and rapidly declining levels of real consumption also contributed. At the same time, Canadian exports of transportation equipment remained strong throughout the period and were augmented by increased levels of crude petroleum exports. Thus the nominal level of exports held up during the period, while that of imports declined considerably.

A further factor was the impact of declining interest rates on debt-servicing costs. Despite a rapid increase in external-debt stocks, the level of payments did not increase proportionately because of the fall in interest rates. While the service account deficit increased by nearly $3.5 billion between 1980 and 1981, the increment was reduced to just over $2 billion between 1981 and 1982. Thus the negative pressure from the service account on the current account balance was not as severe in 1982. In summary, we see a current account position that swung from a deficit of 1.9 per cent of GNE in the second quarter of 1981 to a surplus of 1.2 per cent in the fourth quarter of 1982.

Looking Ahead

Although the look into the future is more pleasant than the experience of the recent past, one must be careful when interpreting near-term projections that incorporate a recovery path, because of the low base from which the growth rates are derived. For example, we expect real growth during the 1983-85 period to average a little below 4 per cent per year, but the level of real GNE will not exceed the peak that occurred in the second quarter of 1981 until the early or middle part of 1984. Thus it will take four to six quarters after the turnaround in early 1983 just to return to the level attained in 1981. During the recovery period the use of physical and human resources will improve, but there will be areas where resources remain underutilized.

The outcome for the medium run (1985-87) depends on a number of factors, some of which are beyond the control of Canadians. For example, the course of interest rates and the timing, strength, and durability of the recovery in the United States are critical for Canada. Variations in domestic monetary policy, the personal saving rate, and the timing of new investments, as well as continued wage restraint or the appearance of a wage bubble, could also influence the outlook for this country. The assumptions made in developing our base case projection of medium-term economic developments take these considerations into account.

The External Environment

Generally speaking, the news on the economic situation in the United States is also good. There are many positive indications that the U.S. economy is now undergoing a healthy recovery. We anticipate that real growth rates will range between 3.0 and 5.3 per cent over the 1983-85 period, averaging 3.1 per cent annually in the medium run (Table 3-5). The initial characteristics of the U.S. recovery are similar to those which we expect for Canada, reinforcing the notion that it is the North American economy that is recovering from a set of common problems. In the initial stages of the recovery, housing and consumer durables will be major contributors. Later, business fixed investment will also take on more importance. During the final stages, there may be a period of stock adjustment, which could contribute to a pause just after mid-decade. This would lead to a slowdown in growth in Canada during the same period.

The recovery in the United States was helped early on by expansion in home-building activity. This was reinforced by consumer demand, especially for durable goods and, more specifically, for automobiles. The average age of the stock of autos in the United States at the end of 1982 was higher than at any time since the Second World War. This, along with lower energy prices, stimulated the demand for automobiles. Recently, consumers in the United States have begun to participate in other markets, and the factors mentioned above, plus the availability of reasonable credit and the anticipation of price stability, should provide a solid basis for this expanded activity.

We do not anticipate nonresidential investment in the United States to pick up substantially until 1984. In 1984-85 some strength should develop in manufacturing durables and nondurables, high-technology communications services, and mining. Mining will be influenced by the decontrol of natural gas in 1985-86, as this will accelerate the shift towards coal.

The outlook for inflation in the United States during the recovery period is very encouraging. We expect growth in consumer prices to average about 3.5 per cent per year during the 1983-84 period and about 5.9 per cent during the 1985-87 period. The inflation that creeps into the system at mid-decade is associated with the deregulation of natural gas prices in the United States and with the upward pressure exerted by commodity prices on world markets, especially crude petroleum, as demand increases.

The Reagan Administration and the U.S. Congress are currently struggling with an anticipated record budget deficit for the next fiscal year. We have assumed that President Reagan's budget will pass, but only after it has been modified to include some reduction in the planned increase of 7 per cent in defence spending; a rejection of the pay freeze, with federal pay raises ranging between 4 and 5 per cent; no further cuts in means-tested social programs; some changes in nondefence and grants-in-aid

Table 3-5

External Environment Assumptions (Base Case Projection), 1983-87

	1983	1984	1985	1986	1987
			(Percentage change)		
Industrial production					
OECD area	2.6	6.2	5.2	0.9	3.9
Selected OECD countries[1]	1.2	3.3	2.8	2.1	2.1
International price of crude petroleum (f.o.b., $ Can.)	-11.6	4.9	5.7	5.7	6.2
United States					
Real gross national expenditure	3.0	5.3	4.4	0.8	4.1
Industrial production	3.4	7.7	6.4	0.4	4.7
Consumer price index	2.6	4.5	6.2	5.5	6.0
			(Per cent)		
Unemployment rate	10.0	8.9	7.8	8.6	7.8
Short-term interest rate[2]	8.3	8.4	8.8	7.7	8.1

[1] France, Italy, West Germany, the United Kingdom, and Japan.
[2] Short-term prime commercial paper rate.
SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

expenditures; and implementation of the 1983 personal tax cut as scheduled but with a subsequent repeal of the indexation of personal taxes before it becomes effective in 1985. Admittedly, these assumptions are tenuous. They do, however, reflect U.S. views and imply a federal deficit that will approach $200 billion in 1983, with a reduction to $126 billion by 1987.

Monetary policy in the United States can be characterized in much the same way as we have described the approach taken by the Bank of Canada. The Federal Reserve Board is seeking to avoid credit conditions that might cause overshooting on either the up side or the down side. Because a favourable inflationary performance is anticipated during the early stages of the recovery, short-term prime interest rates are expected to be in the 8 to 9 per cent range in 1983-84. As upward inflationary pressures are projected for mid-decade, we anticipate that neither long- nor short-term rates will decline much further.

The U.S. recovery will not be without problems. We anticipate that the unemployment rate will average 10 per cent in 1983 and that it will not fall below 8 per cent until 1985. Nor is it clear how financial markets will react to the very large federal deficits that must be financed in the medium run, especially during the early stages of recovery. At this time, it appears that these deficits can be handled by financial markets without upward pressure on short-term rates. One must remember that in the early stages of the recovery our estimates of nominal interest rates and inflation rates imply high real rates. Thus these large deficits are accompanied by tight credit conditions when viewed in this perspective.

Industrial production in the OECD countries will follow a path similar to that in North America: the rates for 1984 and 1985 will be above trend; 1986 and 1987 will be years of readjustment, with 1986 being weak but positive. The major problem in the OECD countries outside North America will be unemployment, which will remain high during the recovery period.

Energy Supply, Demand, and Price

The weakness in the world demand for oil, brought about by slow real growth in the early 1980s, has led to a softening of world oil prices, with Saudi Arabian light crude having settled at $29.00 (U.S.) a barrel in early 1983. These soft market conditions, which are still prevalent, will give rise to a stable international pricing regime until mid-decade. We assume that, with most of the oil-exporting countries now in need of cash, supply will be maintained and the international price will not change (in real terms) in 1984-85; thereafter we assume that demand pressures will eventually bring about the resumption of real gains for OPEC and other oil producers and that the international price will increase by 0.5 per cent a year in real terms in 1986-87.

We assume that the domestic wellhead price for conventional oil will average $29.75 in 1983, as set down in the June 1983 amendment to the Ottawa/Alberta Energy Agreement (Table 3-6). The wellhead price will remain at this level until there is sufficient movement in world prices to permit further adjustments. Any such adjustment will be subject to the political decision that the Canadian wellhead price (plus transportation costs) must not exceed

Table 3-6

Components of the Domestic Crude Petroleum Price to Consumers (Base Case Projection), Canada, 1983-87

	1983	1984	1985	1986	1987
			(Dollars per barrel)		
Domestic price at Toronto	35.55	36.85	38.55	40.95	43.74
Canadian ownership charge[1]	1.15	1.15	1.15	1.15	1.15
Petroleum compensation charge[2]	3.51	4.76	6.08	6.73	7.52
Transportation charge[3]	1.14	1.19	1.25	1.31	1.37
Wellhead price for conventional old oil[4]	29.75	29.75	30.07	31.76	33.70
International price at Montreal	37.36	39.16	41.35	43.65	46.30
Ratio of domestic wellhead price to international price	0.821	0.783	0.750	0.750	0.750

1 Assessed at $1.15 per barrel for the period from May 1981 to the end of the projection period.
2 The petroleum compensation charge reflects a shift to "new" oil, as well as to the continued softening of world prices early in the period.
3 To Toronto only.
4 As per the June 1983 amended agreement between Ottawa and Alberta.
SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

75 per cent of the world price at Montreal. That rule, of course, is not immutable. Nevertheless, throughout the remainder of the projection period the domestic wellhead price is assumed to increase at the same rate as the world price, with the 75 per cent cap as a limit. The reference price for new oil is set at 100 per cent of the international price at Montreal (less transportation costs). It is applied to many categories of new oil (oil found after 1980) as well as the redefined category of "new" old oil. On the strength of the April 1983 federal budget, we maintain the "Canadian ownership charge" of $1.15 per barrel for the entire projection period. The domestic price at Toronto will differ from the wellhead price by the amount of the transportation costs, the Canadian ownership charge, and the "petroleum compensation charge." Revenues from the latter will be used to subsidize imports and the production of new oil and new "old" oil.

Natural gas prices at the wellhead will increase at the rates laid down in the amendment to the energy agreement. Because of the weakness of world oil prices and the resulting low rates of growth of domestic wellhead prices, the 65 per cent parity relationship between the prices for domestic natural gas and for oil is maintained in our assumptions by reducing the increments to the wellhead price. Beyond 1984, however, the increments take precedence over the 65 per cent parity relationship, bringing the domestic wellhead price for natural gas to an average of 75 per cent of the domestic wellhead price for oil during the 1985-87 period.

There are a number of energy tax measures included in the assumptions. The April 1983 budget repealed the marine and aviation fuel tax as of the end of that month; consequently, revenues from that source fall to zero from that moment onward. As previously indicated, the Canadian ownership charge will be maintained during the entire projection period, not only for oil but also for natural gas. The revenues that result (about $900 million per year) will be used to help meet the government's stated energy objectives, such as the purchase of Petrofina and the federal contribution to the financial restructuring of Dome Petroleum. Revenues from the tax on natural gas and gas liquids will disappear after 1983 because the scheduled increases in the wellhead price of natural gas, when combined with the oil prices set in the June 1983 amendment, will leave no room for the tax. As indicated in the April 1983 budget, the exemption of conventional old oil from the incremental tax on oil revenues is extended from May 1983 to May 1984.

The oil supply assumptions for conventional reserves that are used in the base case are those of the National Energy Board (NEB). For reserve additions, we have used the more optimistic NEB projections associated with the National Energy Program update. These supply estimates for the projection period include small amounts of oil from the Hibernia field by 1986 but none from the Alsands or Cold Lake projects (Table 3-7). We have also included the Syncrude partial extension. As well, the Canstar project is assumed to go ahead, but production will not have any impact on the supply projection, because it will not come on stream until the late 1980s. The natural gas supply assumptions are taken from the estimates issued after the 1982 Export Omnibus Hearings; however, all supplies are assumed to originate from conventional nonfrontier areas. The TQM Pipeline to Quebec and the Maritimes is assumed to be completed by 1985, with the tag ends to be finished by 1987. We have also made appropriate adjustments to bring consistency between our projections of energy investment and the measures introduced in the April 1983 budget. The extension of the 7 per cent investment tax credit to heavy construction equipment has been taken into account in our energy investment projections.

We have incorporated a demand profile for crude petroleum that implies a decline of just under 1 per cent a year after a substantial reduction in the 1981-83 period. This contrasts with the demand for

Table 3-7

The Phasing of Large-Scale Energy Investment Projects (Base Case Projection), 1983-92

	Phase-in year	Peak period	Phase-out year
Oil sands			
Syncrude partial extension	1983	1986-87	1988
Canstar	1986	1989-90	1991
Cold Lake[1]	1991	. . .	. . .
Alsands[2]	. . .	. . .	. . .
Pipelines			
TQM pipeline	1981	1982-84	1987
Alaska Highway gas pipeline	1985	1986-87	1990
East Coast gas pipeline	1989	1990-91	1992
Hibernia oil project	1985	1986-87	1988

1 The peak period and phase-out year of the Cold Lake project are assumed to occur beyond the projection period.

2 The Alsands project has been excluded from the energy assumptions.

SOURCE Economic Council of Canada, CANDIDE Model 2.0, July 20, 1983.

natural gas, which is assumed to increase at a rate close to 3.5 per cent annually. The natural gas export assumptions include sales of liquid natural gas to Japan in the latter part of the 1980s. If our projections are stretched to the end of the decade and beyond, they imply self-sufficiency by 1990, with lower import levels in the 1983-90 period.

Fiscal and Monetary Policy

The April 1983 budget contained a number of changes in the federal government's taxation and spending policy, which we have incorporated into the base case projection (Table 3-8). These measures include: the Special Recovery Program, totaling $4.8 billion in federal spending; changes in the existing legislation associated with the investment tax credit, which not only make the latter more attractive but also extend its coverage to investment in heavy construction equipment; certain changes in corporate taxation, leading to revenue losses to the federal government; and changes in personal and indirect taxation that involve revenue gains for the federal government, although most of them do not take effect until late 1984. We have also taken into account other budget changes, including the telecommunications programming service tax, changes in duty-free import limits, and changes in taxation on alcohol and tobacco. We should point out that the fiscal measures associated with the November 1981 and June 1982 budgets, with the Established Program Financing arrangements for the 1982-87 period, and with the "6 and 5" program for 1983-84 are also part of our assumption set. All other federal programs are assumed to remain as currently legislated.

In the base case projection, it is assumed that money supply growth will contribute to a stable recovery. Because of the rapid declines in velocity in recent years, growth in the money supply will exceed the rate of growth of nominal GNE in the near term. During the recovery period these temporary changes are viewed as necessary to ensure a balance in the domestic financial markets and the foreign-exchange markets. In the medium term, the pattern for money supply growth will be consistent with the position taken by both the Bank of Canada and the U.S. Federal Reserve Board. Consistency will remain between the rate of growth of the money supply and that of nominal GNE, once the downward shift in velocity stabilizes. As a result, real rates of interest and the exchange rate will vary little from current values.

Taking all these factors into account, we turn to the highlights of the base case projections for the period from 1983 to 1987 (Table 3-9).

Table 3-8

Domestic Policy Assumptions in the Base Case

Energy pricing	**Crude petroleum and natural gas pricing schedules are as per the 1981 energy pricing agreements and subsequent agreements, with revenues split between producing provinces, the federal government, and producers in accordance with the most recent policies.**
Tax policies	**All post-budget (November 1981, June 1982, and April 1983) tax schedules (personal, corporate, and indirect) are in place, including schedules incorporating the 1981 energy agreements, the National Energy Program, the NEP Update and the June 1983 energy agreement amendment,where applicable. This includes the petroleum compensation charge, the Canadian ownership charge, the incremental oil revenue tax, the natural gas and gas liquids tax on domestic production, and the petroleum and gas revenue tax. The Quebec personal income tax remains a constant portion of total provincial taxes. All provincial budgets, as of April 1983, are incorporated.**
Expenditure policy	**Government spending on goods and services is restrained, with annual increases in real expenditures averaging as follows: federal government - nondefence, 2.2 per cent, and total defence, 2.1 per cent; provincial governments - wages and salaries, 2.4 per cent, and other spending, 1.5 per cent; municipal governments - wages and salaries, 0.7 per cent, and other spending, 1.5 per cent. Government wages are indexed to increase in line with the CPI, except for federal wages, which follow the 6 and 5 per cent rule for 1983 and 1984. Transfer payments are indexed as legislated. Established Program Financing and fiscal arrangements reflect budget changes and the five-province standard for equalization payments. Federal spending associated with capital assistance and subsidies reflects existing government policy. Among other things, allocation to the economic development and energy envelopes is as outlined in the recent budget papers.**
Monetary policy	**Canadian interest rates are in line with U.S. rates. The money supply is accommodating, with temporary downward movements in velocity accounted for.**

SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

Table 3-9

Selected Economic Indicators (Base Case Projection), Canada, 1983-87

	1983	1984	1985	1986	1987
	(Percentage change)				
Gross national expenditure (1971$)	2.9	4.3	3.9	1.8	2.6
Consumer price index	5.7	4.8	5.1	5.9	6.7
Labour force	1.8	1.9	1.7	1.6	1.4
Employment	0.6	2.4	2.2	1.3	1.8
Productivity[1]	3.1	2.4	2.4	1.2	1.6
Real wage rate	1.8	1.2	2.8	2.6	2.2
Nominal wage rate	7.6	6.0	8.0	8.7	9.0
	(Per cent)				
Participation rate[2]	62.6	63.1	63.4	63.6	64.0
Saving rate[3]	12.6	12.5	12.0	11.0	11.0
Unemployment rate	12.1	11.7	11.2	11.4	11.1
	(Percentage of GNE)				
Real investment	20.9	20.8	21.3	21.9	22.1
Federal surplus or deficit (-)	-6.9	-6.7	-5.3	-4.1	-4.0
Provincial surplus or deficit (-)	-0.6	-0.5	-0.2	0.1	0.3
Balance of international payments					
Current account	0.5	-0.3	-0.3	-0.3	-0.3
Energy	1.8	1.9	2.2	2.5	2.7
Nonenergy	-1.4	-2.2	-2.5	-2.8	-3.1

1 Output per person-hour.
2 Labour force as a proportion of the population aged 15 and over.
3 Personal savings as a proportion of personal disposable income.
SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

Highlights of the Base Case

During the 1983-85 period real growth in Canada will average about 3.7 per cent; that growth pattern will carry the Canadian economy past the 1981 second-quarter peak in early or mid-1984. During the 1985-87 period real growth will average about 2.8 per cent – about 1 percentage point less than during the recovery years.

During the initial stages of the recovery there will be some decline in the unemployment rate, because the annual rates of real growth will exceed long-run potential growth by just under 2 percentage points. This pattern will be short-lived, however; in the absence of new initiatives, the unemployment rate is not expected to decline further later on in the projection period. Growth in employment during the recovery period will be substantial. Later, however, employment and labour force growth will follow similar patterns, implying no further reduction in the unemployment rate.

Inflation performance during the recovery period will be very encouraging. The rate of growth of the CPI during the 1983-85 period will average about 5.2 per cent. It will rise slowly over the 1985-87 period, averaging close to 6 per cent per year. Pressures from foreign prices, particularly those associated with the decontrol of natural gas prices in the United States, will put upward pressure on Canadian prices.

Productivity growth during the recovery period will be above its long-run trend. That strong performance will be influenced not only by improvements in the utilization of labour and capital but also by changes in the mix of final demand. Construction and consumer durables – traditionally high-productivity sectors – will be early contributors to this improvement. Housing starts, for example, are expected to average about 175,000 units at annual rates in 1984 – approximately 40,000 units below the demographic requirements in a medium-run context. During the 1985-87 period, when the trend growth of real GNE re-emerges at 2.8 per cent, average productivity growth will return to an average between 1 and 2 per cent. This performance will be better than that of the 1970s but not as good as that of the 1960s.

The pattern of the recovery and the level of demand that will be sustained thereafter will depend in part on the path of the personal saving rate. We expect that it will fall only slightly during the recovery period. Later, we anticipate an additional reduction of 1 percentage point.

Real investment as a percentage of GNE in 1984 will not differ much from the outcome in 1983. A modest recovery in nonresidential business investment will not materialize until the 1985-87 period. By 1987 real investment will approach 22.1 per cent of GNE – only 1.2 percentage points above that anticipated in 1983.

The federal government will remain in deficit during the entire projection period. During the recovery period, however, the federal deficit as a percentage of GNE will be reduced from a high of 6.9 per cent to 5.3 per cent by 1985 and to about 4 per cent by 1987. Provincial governments will return to a surplus position after mid-decade.

From its present surplus position, the current account of Canada's balance of payments will move slightly into deficit during the projection period. The surplus in the energy current account resulting from the increased licensing of natural gas exports to the United States and Japan and from lower crude petroleum imports will just balance the nonenergy deficit.

Growth in the money supply will accommodate the decline in velocity anticipated in the near term. In 1985 the downward shift in velocity will moderate and then stabilize during the 1986-87 period. This performance will contribute to a stable recovery, with little or no change in real rates of interest and/or the exchange rate.

Sources of Uncertainty

Our best judgment about the factors that will shape future economic events – present government policy (as embodied in the envelope allocation and taxation package presented in the April 1983 budget), the evolution of the economies of the United States and the other major OECD countries, and the outlook for energy demand, prices, and investment, as well as for world commodity prices – envisions that recovery in Canada will weaken and falter after only 12 quarters, before any substantial dent is made in the unemployment rate. According to our projections, the Canadian economy will not fall back into recession, but real growth will decline to below 2 per cent annually in 1986.

Although there is good reason to regard this path as the most likely, it has to be said that our base case assumptions represent a number of judgments that embody considerable uncertainty. For example, as it stands now, the base case projection shows weakness in 1986, in part because the recovery in the United States is expected to stall that year – as a result of strong inventory decumulation and of a drop in the growth of real income caused by the decontrol of natural gas prices – and in part because the resurgence in domestic investment spending never gains momentum, as a result of the persistence of high real rates of interest during the 1984-86 period. These are perhaps the most worrisome aspects of the base case projection. The weakening anticipated in the United States in 1986 could, however, degenerate into a more serious slowdown that could come earlier and be more severe if the external-debt problems of a number of South American and eastern European countries were to lead to a financial crisis for the international banks or to a severe restriction of the credit needed for international commerce. Or the weakening could turn out to be less severe than envisaged, especially if the debt problems are managed expeditiously.

In the area of monetary policy, nominal interest rates in both the United States and Canada have fallen dramatically since mid-1982 as a result of, among other things, the deceleration in inflation, the weak demand for credit, and the easing of monetary restriction in both countries. In the medium term, the steady decline in the rate of inflation is projected to produce a moderate decline of 1 percentage point in nominal interest rates. But real interest rates (especially long-term) are expected to remain high, averaging between 5 and 6 percentage points. This outcome is in line with anticipated high government deficits, especially in the United States. However, there remains a degree of uncertainty about medium-run monetary policy in the two countries. In an effort to strengthen the prospects for output and employment growth, both the U.S. Federal Reserve Board and the Bank of Canada could decide to ease monetary policy even if that were to cause a little more inflation. On the other hand, the pressures exerted on interest rates by deficit spending could be stronger than is implied in the base case. In addition, the Bank of Canada might choose to influence the pattern of Canadian interest rates independently of developments in the United States, thereby causing some external pressures in foreign-exchange markets.

Another source of uncertainty is the behaviour of consumers in the medium term. Consumer spending during the initial stages of the recovery, especially on durable goods and housing, will be supported not only by growth in real incomes but also by a significant decline in the personal saving rate from the high levels attained during the recession. In the base case, the personal saving rate is expected to decline, stabilizing at a much higher level (11 per cent) than that recorded in the 1970s. This outcome is reasonable, in view of the expected large government deficits, high real interest rates, high unemployment rates, and continued inflationary pressures. However, consumers may react more favourably to reductions in the inflation rate and to employment growth than is suggested in the base case. On the other hand, continued high levels of unemployment and real interest rates could result in a higher personal saving rate than is implied in the base case.

Similarly, both the strength and the durability of the recovery depend on the regeneration of a healthy setting for investment spending. Although energy investment is fairly strong in the base case, nonenergy investment is not as buoyant. This modest recovery is consistent with high real rates of interest, low capacity-utilization rates, and a weak recovery in aggregate demand.

The combination of weak demand, moderation in both energy and raw-material prices, and the government-sector wage restraint program has slowed down both wage and price increases since mid-1982: the year-over-year increase in the CPI in June 1983 was 5.6 per cent. In the base case, the inflation rate is expected to decline from nearly 11 per cent in 1982 to slightly below 5 per cent in 1984. Similarly, wage increases will fall from about 12 per cent to 6 per cent over the same period. This anticipated performance is consistent with wage restraint in the public sector, continued slack in labour markets, and only moderate increases in both export and import prices. During the 1985-87 period wage and price inflation will be subject to some acceleration, as the result of mounting pressure from international commodity prices and from above-average growth in the money supply during the 1983-85 period. We do not regard this outcome as certain, however. For example, continued wage restraint in the government sector could have a greater demonstration effect than we have anticipated on wage behaviour in the private sector, resulting in more rapid deceleration of wage price inflation than indicated in the base case. Continued slack in the labour market could also provide more optimism for further wage deceleration. On the other hand, once the economy recovers from the recession and the present wage restraint program is terminated, wages and prices could revert to a catch-up attitude.

Variations to the Base Case

Because of these uncertainties, it is useful to assess the impact of factors that could emerge as significant but that are not part of the assumption set or of the outcome of the base case (Table 3-10):

Table 3-10

Alternative Scenarios for Selected Indicators, 1983-87

	1983	1984	1985	1986	1987
			(Percentage change)		
Gross national expenditure (1971$)					
Base case	2.9	4.3	3.9	1.8	2.6
U.S. high growth	2.9	4.4	4.0	2.7	3.1
U.S. low growth	2.9	4.5	3.2	1.2	1.9
U.S. high interest rates	2.9	4.4	3.1	1.7	1.9
U.S. low interest rates	2.9	4.2	4.5	2.5	3.0
High Canadian interest rates	2.9	4.4	3.7	1.7	2.5
Low Canadian interest rates	2.9	4.3	4.2	1.9	2.9
High investment	2.9	5.8	3.8	1.7	2.6
Low investment	2.9	2.9	4.1	1.9	2.7
High wage growth	2.9	4.6	4.2	2.2	3.1
Low wage growth	2.9	4.1	3.6	1.4	2.2
High saving rate	2.9	3.5	4.0	1.9	2.7
Low saving rate	2.9	5.3	3.9	1.7	2.6
Consumer price index					
Base case	5.7	4.8	5.1	5.9	6.7
U.S. high growth	5.7	4.8	4.9	5.7	6.6
U.S. low growth	5.7	5.6	5.8	7.4	7.9
U.S. high interest rates	5.7	5.5	5.6	6.8	7.2
U.S. low interest rates	5.7	4.3	4.7	5.4	6.4
High Canadian interest rates	5.7	4.4	4.7	6.0	6.9
Low Canadian interest rates	5.7	5.2	5.4	5.8	6.6

Table 3-10 (Concl'd.)

	1983	1984	1985	1986	1987
			(Percentage change)		
High investment	5.7	4.9	5.2	5.9	6.7
Low investment	5.7	4.7	4.9	5.9	6.8
High wage growth	5.7	5.5	6.3	7.5	8.5
Low wage growth	5.7	4.0	3.8	4.3	5.0
High saving rate	5.7	4.8	5.0	5.8	6.8
Low saving rate	5.7	4.8	5.1	6.1	6.7
			(Per cent)		
Unemployment rate					
Base case	12.1	11.7	11.2	11.4	11.1
U.S. high growth	12.1	11.6	11.2	11.1	10.6
U.S. low growth	12.1	11.4	11.0	11.1	11.0
U.S. high interest rates	12.1	11.5	11.2	11.2	11.3
U.S. low interest rates	12.1	11.8	11.3	11.4	10.9
High Canadian interest rates	12.1	11.6	11.2	11.3	11.0
Low Canadian interest rates	12.1	11.7	11.2	11.5	11.2
High investment	12.1	11.1	10.6	10.8	10.5
Low investment	12.1	12.2	11.8	12.0	11.7
High wage growth	12.1	11.7	11.3	11.6	11.3
Low wage growth	12.1	11.6	11.0	11.2	10.9
High saving rate	12.1	12.0	11.6	11.9	11.6
Low saving rate	12.1	11.3	10.8	10.9	10.7
Federal government balance			(Percentage of GNE)		
Base case	-6.9	-6.7	-5.3	-4.1	-4.0
U.S. high growth	-6.9	-6.7	-5.2	-3.9	-3.5
U.S. low growth	-6.9	-7.1	-6.1	-5.4	-5.5
U.S. high interest rates	-6.9	-7.1	-6.0	-4.9	-4.8
U.S. low interest rates	-6.9	-6.5	-4.8	-3.6	-3.3
High Canadian interest rates	-6.9	-7.1	-6.0	-4.8	-4.9
Low Canadian interest rates	-6.9	-6.3	-4.7	-3.4	-3.2
High investment	-6.9	-6.3	-4.9	-3.7	-3.7
Low investment	-6.9	-7.1	-5.7	-4.5	-4.4
High wage growth	-6.9	-6.6	-5.1	-3.8	-3.6
Low wage growth	-6.9	-6.8	-5.5	-4.4	-4.4
High saving rate	-6.9	-7.0	-5.6	-4.4	-4.3
Low saving rate	-6.9	-6.4	-5.0	-3.8	-3.7
Current account balance of international payments					
Base case	0.5	-0.3	-0.3	-0.3	-0.3
U.S. high growth	0.5	-0.3	-0.2	-0.2	-0.1
U.S. low growth	0.5	-0.7	-0.5	-1.0	-0.7
U.S. high interest rates	0.5	-0.7	-0.5	-0.7	-0.5
U.S. low interest rates	0.5	-0.2	-0.2	-0.1	-0.1
High Canadian interest rates	0.5	-0.6	-0.8	-0.9	-0.9
Low Canadian interest rates	0.5	-0.1	0.2	0.2	0.2
High investment	0.5	-0.9	-0.7	-0.7	-0.7
Low investment	0.5	0.2	0.2	—	—
High wage growth	0.5	-0.4	-0.4	-0.6	-0.7
Low wage growth	0.5	-0.3	-0.2	-0.1	0.1
High saving rate	0.5	—	0.1	—	-0.1
Low saving rate	0.5	-0.7	-0.6	-0.6	-0.6

SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

- A more durable recovery in the United States would eliminate the growth pause in 1986, add about $2.5 billion to real GNE by 1987, and help to reduce the federal deficit. A less robust U.S. situation would weaken the projected Canadian performance during the 1985-87 period and make more immediate the need for policy action.

- A tighter U.S. monetary policy would reduce investment spending in this country if Canada were to follow suit. By weakening an already lacklustre investment picture, it could abort the Canadian recovery. A more accommodating monetary policy would permit more growth in areas where it is needed (investment) and reduce debt-servicing costs, thus lowering the federal deficit. If it were too accommodating, however, it could contribute to upward pressure on prices.

- A more robust investment picture originating autonomously would produce a number of important benefits, including higher growth, lower government deficits, and improved productivity performance. If real interest rates were lowered unilaterally in Canada, the Canadian dollar would be subjected to downward pressure.

- If the rapid decline in the personal saving rate continues, it could provide additional support to the recovery. If consumers were to show reluctance, however, in the form of a higher personal saving rate than that contained in the base case, this could place a heavier burden on governments to maintain the momentum of the recovery.

- A wage bubble originating from an increase in price expectations of only 2 percentage points above the base case figure could put Canada back on an inflation path that could easily lead to double-digit rates by the end of the decade. Continued wage restraint without price restraint could reduce real wages, resulting in slightly lower growth for output and employment. However, other factors could intervene to counteract the negative effects of such potential developments. For example, declining (or rising) rates of inflation could be accompanied by personal saving rates that fall (or rise) at a slower pace than in the base case.

The base case characteristics can be altered in varying degrees by considering each of these alternatives individually. It is also useful to combine a

Table 3-11

Alternative Projections, 1984-87[1]

	1984	1985	1986	1987
		(Percentage change)		
Gross national expenditure (1971$)				
Base case	4.3	3.9	1.8	2.6
Optimistic alternative	+1.3	+0.3	+1.2	+0.9
Pessimistic alternative	-0.9	-1.0	-0.9	-1.1
Consumer price index				
Base case	4.8	5.1	5.9	6.7
Optimistic alternative	+0.7	+1.1	+1.5	+1.6
Pessimistic alternative	--	-0.6	-0.2	-0.5
		(Thousands)		
Employment				
Base case	10,670.4	10,906.2	11,050.0	11,244.9
Optimistic alternative	+52.6	+75.0	+139.7	+192.5
Pessimistic alternative	-32.5	-75.0	-98.9	-154.8
		(Percentage of GNE)		
Federal government balance				
Base case	-6.7	-5.3	-4.1	-4.0
Optimistic alternative	+0.4	+0.6	+0.8	+1.1
Pessimistic alternative	-0.8	-1.4	-2.1	-2.3
Current account balance of international payments				
Base case	-0.3	-0.3	-0.3	-0.3
Optimistic alternative	-0.4	-0.4	-0.4	-0.4
Pessimistic alternative	—	+0.2	-0.2	+0.2

[1] The values for the optimistic and pessimistic alternatives are expressed as additions to, or subtractions from, the base case values. The optimistic assumptions include high U.S. growth, high wage growth, and low saving rate. The pessimistic assumptions include low U.S. growth, low wage growth, and high saving rate.

SOURCE Economic Council of Canada, CANDIDE Model 2.0, August 1983.

number of them (Table 3-11) so as to highlight the base case results. For example, one might consider the combination of higher U.S. growth, higher domestic wage growth, and a lower domestic personal saving rate. Such a scenario would generate a higher rate of real growth; we label it the "optimistic real-growth alternative." An alternative to this would be an outcome that would include lower U.S. growth, lower domestic wage growth, and a higher domestic personal saving rate. This is labeled the "pessimistic real-growth alternative."

The pessimistic alternative provides for a loss of about 1 percentage point in real growth each year from 1984 to 1987, while the optimistic alternative provides for a gain of about 1 point. Both scenarios have good and bad points. The optimistic alternative is accompanied by increased employment opportunities and smaller government deficits as a percentage of GNE, but also by a deterioration of inflation and the current account balance. The pessimistic alternative entails reduced employment opportunities, lower inflation, larger government deficits relative to GNE, and an improved current account balance. In both scenarios, the federal deficit is very sensitive to some of the more important judgments included in the base case.

Some Critical Issues

Is the Federal Deficit Cyclical or Structural?

The base case projection and its variants could lead one to believe that the federal government, because of the magnitude of its deficit, is constrained in the amount of additional support that it can give to the recovery and to medium-run performance. In assessing the medium-term implications of the federal deficit for interest rates and investment spending, however, a number of additional issues must be considered, such as the degree of slack in the economy, the behaviour of investors, the accounting distortions that may result during periods of inflation, and the budget positions of the other levels of government.

At the same time, many government and business leaders, and some economists, have expressed concern that debt repayment constitutes a real burden and that there is a limit to the amount of indebtedness that governments can carry. Others remain more sanguine, arguing that, at least for that part of the public debt that is held by Canadians, there can be no burden since it is money that we owe ourselves and since, given their taxing powers, governments are unlikely to go bankrupt.

While it is true that the domestic debt does not impose an immediate burden on Canadians, it does tax future generations: by borrowing today, Canadian governments exchange future purchasing power (represented by the bonds and the interest thereon) for cash. When the bonds are repaid, the future taxpayers who foot the bill under compulsion may well feel a sense of loss.

As for the foreign debt, clearly it is not money that we owe ourselves but a burden on future generations. If they pay back the loan and interest in foreign currencies, they will have to earn this money by exporting and by retaining fewer goods for their own consumption. If the debt is paid in Canadian dollars, foreign bond holders also gain command over Canadian goods, which they will ultimately exercise.

Thus a burden is imposed on future generations of taxpayers when governments borrow in the present, regardless of whether the debt is held by outsiders or by Canadians. It goes without saying, however, that the *net* burden of the debt can be made nil or negative by judicious investment of the borrowed funds. If they are used for beneficent public works that yield more than they cost in interest, that is a good reason to borrow. Nevertheless, the burden remains, since the net yield of the same public works would increase if they were financed by taxes or by equity offerings.

What sets the limit on the amount of the debt? In theory, there is none but the taxing powers of the State. More realistically, the limit is far below that – at a point where the debt burden is so heavy that a large number of taxpayers face objectionably high marginal rates of income tax. But even before that point is reached, government can be using too much credit, leaving too little for the private sector. A nation's accumulated savings and capital tend to be in a fixed proportion to its income (about 3 to 1). If government wants to use a larger proportion of these savings, private industry will have to do with less or to pay higher rates of interest. In effect, therefore, no single figure can be cited as an optimum amount of debt. That amount can vary from time to time and from country to country, depending on the prevailing amounts of private debt, national savings, and capital in relation to income.

At the end of 1982 the federal government's direct and guaranteed debt, including bonds held by the Bank of Canada, amounted to 31 per cent of GNE. That proportion was higher than it was ten years earlier but much lower than in previous times: it was 41 per cent in 1930 and 42 per cent in 1960. Thus, from a historical point of view, it is not clear whether the federal debt is too high. If circumstances today deem that a reduction of the debt is desirable, however, how soon could this reduction come about?

That question is intimately interrelated with the issue of the federal deficit. The interest on the public debt, which affects the level of the deficit, depends on price levels, since governments must pay a set real rate of interest, plus an additional amount for the inflationary erosion of the debt instrument's purchasing power. Deficits naturally increase the debt outstanding. Surpluses, on the other hand, not only reduce it but give government the opportunity to earn more money by "investing" in its own bonds. The actual course over time of deficits, the debt, and inflation will depend on the rates of growth of national income, government expenditures, and taxes. Simple numerical examples can be constructed on the basis of different sets of assumptions for these variables.

As a first approximation, suppose that in each period the central bank purchases just enough government bonds to increase the money supply at a rate of growth equal to that of real GNE, without regard to the level of the deficit or surplus. If one also assumes that real income grows at 2 per cent per year; that real government expenditures, while growing absolutely, fall in relation to income by 0.75 per cent per year; that the ratio of tax revenue to income rises by 0.85 per cent per year; and that the real rate of interest is 3.6 per cent, the deficit will turn into a surplus by the eleventh year. The debt/income ratio will rise for nine years and fall back to its initial level by the seventeenth. At its peak, it will be 70 per cent higher than it was at the beginning. The inexorable rise of the debt ratio can thus be seen as a troublesome feature for some time to come. One cannot escape the fact that the debt grows whenever there is a deficit that swells at a faster rate than that of real income itself.

Under most circumstances, the degree of fiscal restraint or stimulus that the federal government imparts to the economy is directly related to the size of its deficit – i.e., the difference between the tax revenues that it collects and the spending levels associated with the activities in which it engages. Assessment of the impact of the government's fiscal position also involves such questions as how the deficit is financed and how it is measured. There are a number of ways to measure the government deficit. In the base case projection, we have used the difference between revenues and spending, as calculated on a National Accounts basis – what is referred to as "the National Accounts deficit."[4] Use of this approach permits an examination of the interaction between the public and other sectors of the economy, and it is specifically designed to focus on economic impact.

In determining the fiscal stance of the government, one must also consider the distortion that inflation can cause in the way that financial markets handle the deficit. This distortion occurs because, during a period of inflation, the debt-servicing costs (the interest payments on the public debt) include a premium for anticipated inflation. Holders of government debt or, for that matter, any financial instrument demand not only a return that is competitive in real terms but also a premium over and above that rate of return, to compensate for any damage that inflation is expected to inflict on the real value of the asset while it is held. In the financial literature, this premium has been labeled "the inflation premium" or "the capital repayment factor."[5] The value of the capital repayment factor is related to neither a social nor a private real rate of return. It is determined solely by the market's assessment of anticipated inflation. As inflation abates, the premium declines, and so does the cost of servicing the public debt. That, in turn, works to reduce the deficit.

The portion of the deficit that is attributable to the capital repayment factor can be easily financed in financial markets if government bond holders recycle the premium into more bonds of the same kind, in order to ensure that the real value of their financial assets is maintained even during periods of rapid inflation. The recycling may only be partial, as its extent depends on the degree of confidence with which investors can anticipate inflation, on the impact of inflation on the relative yields and risks of various financial and real assets, and on the resulting portfolio choices.

The implication, however, is that part of the debt-servicing costs will find their way directly back to borrowers, as lenders attempt to maintain the real value of their assets. Consequently, the amounts of the anticipated deficits are not the best measure to use when assessing their true immediate and future impact on financial markets. It would be more useful to develop an inflation-adjusted measure. If we want to remove the impact of inflation from the deficit, the capital repayment cost must be netted out. If we want to assess the pressures exerted by deficits on financial markets, only that portion of the capital repayment cost which is recycled by investors into government bonds should be netted out. If, following such an adjustment, the budget is in balance, the financing of the deficit will not present any problems. Should a deficit remain, financing through borrowing will lead to upward pressures on interest rates.

To illustrate, we have assumed that the total capital repayment costs are recycled into government bonds, and we have applied our methodology to the years 1983 through 1987 (Table 3-12). The National Accounts deficit that we anticipate for 1983 is close to $27 billion. After adjusting for inflation, that figure

Table 3-12

Inflation Adjustment (on a National Accounts Basis) to Federal Government Budget Balance, 1983-87

	Government financing requirements	Inflation expectations	Net liabilities	Decrease in the real value of net liabilities	Actual budget balance	Inflation-adjusted budget balance	Actual budget balance	Inflation-adjusted budget balance
	($ Billions)	(Per cent)	($ Billions)	($ Billions)	($ Billions)	($ Billions)	(Percentage of GNP)	
1983	26.3	7.8	86.7	6.8	-26.7	-20.0	-6.8	-5.1
1984	27.9	6.5	113.0	7.3	-28.4	-21.0	-6.7	-5.0
1985	24.3	6.5	140.9	9.2	-24.7	-15.5	-5.3	-3.3
1986	20.2	6.5	165.2	10.7	-20.6	- 9.9	-4.1	-2.0
1987	21.6	6.5	185.4	12.1	-22.0	-10.0	-4.0	-1.8

SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

is lowered to about $20 billion. A similar adjustment for 1987 reduces the National Accounts deficit from about $22 billion to about $10 billion. As a proportion of GNE, the National Accounts deficit in 1983 is about 6.8 per cent, while the inflation-adjusted deficit is about 5.1 per cent; the corresponding figures for 1987 are 4.0 and 1.8 per cent, respectively.

The foregoing calculations are, of course, subject to many qualifications. There are no institutional arrangements in Canada by which the recycling of capital repayments can be made in full and automatically, such as those that exist in some other countries.[6] Moreover, if the target rate of inflation were lower than the one that we have projected, government revenues and expenditures, as well as the inflation-adjusted deficit, could be different from those which are projected, as could other elements of the economy. Considering these qualifications, therefore, inflation adjustments, while useful in interpreting the government's current financial position and past performance, must be used with some caution when discussing future deficits and their financing.

Using the National Accounts framework, how much of the federal deficit can be attributed to the deep recession that occurred in 1981-83? By adjusting both revenues and expenditures for the effects of cyclical conditions, we have obtained an estimate of this component of the deficit, using CANDIDE Model 2.0.

In making this estimate, we have used as the measure of full capacity the "noninflationary level of the unemployment rate," defined as the rate of unemployment that can be achieved without contributing to an acceleration in inflation. Research carried out at the Council and elsewhere suggests that the noninflationary rate of unemployment has not been constant over the last two decades but has risen as the proportion of inexperienced or "peripheral" participants in the labour force has increased. The calculation of this rate is a risky exercise at best. Some estimates are available, however, ranging between 6 and 8 per cent of the labour force. In estimating the cyclical component of the deficit, we have assumed this rate to be 7 per cent. While that figure is well above the levels experienced in the 1960s and the early 1970s, it is about 1 percentage point below the average level in the second half of the 1970s and well below the actual rate of about 12.1 per cent anticipated for 1983.[7]

Our results suggest that the impact of the recent recession on the federal deficit is quite large (Table 3-13).[8] The rule of thumb that we have developed using CANDIDE Model 2.0 suggests that, for each reduction of 1 percentage point in the unemployment rate, the federal deficit decreases by between $2 billion and $2.5 billion. With the average unemployment rates in our base case projection hovering near 11 per cent, a reduction of 4 to 5 percentage points implies that in each of the years from 1983 through 1987 the cyclical component of the deficit is about $10-12 billion per year.

The magnitude of the deficit reduction obtained by applying the cyclical and the capital repayment adjustments to existing and future federal deficits does suggest that the impact of the federal deficit is less than casual observation might suggest. Combining the two adjustments for 1983 suggests that the discretionary federal deficit stands at less than $10 billion. Some may dispute that figure, but the important conclusion to draw from this exercise is that these adjustments lower the deficit considerably. If

Table 3-13

Cyclically Adjusted Federal Government Budget Balance, 1984-87

	Actual budget balance	Cyclical adjustment	Cyclical adjustment
	($ Billions)	($ Billions)	(Per cent)
1984	-28.4	-11.0	38.9
1985	-24.7	-11.0	44.5
1986	-20.6	-12.7	61.8
1987	-22.0	-12.9	58.9

SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

one were to adjust for both cyclical and capital repayment effects, the federal government's budget would be near balance by 1987. Furthermore, if one were to include the provinces in the calculation, the combined balance would be in surplus by 1987.

These crude but illustrative calculations suggest that the federal government will remain in deficit but that those deficits which do occur can be financed more easily than expected without perturbing the financial markets and putting upward pressure on interest rates. Thus in the medium run there may be a margin for manoeuvre to pursue alternative fiscal policies in order to improve performance.

The Real Rate of Interest

Of deep concern to investors, and to Canadians generally in terms of the nation's economic growth potential, is the real cost of borrowing for investment – i.e., the real rate of interest, which is the difference between the market rate and the market's expectation of inflation. If the real rate of interest is low, it encourages risk-taking; if it is high, it can abort new investment decisions. Today, the real rate of interest is at historically high levels. Why?

In an open economy such as Canada's, it is unlikely that monetary management can deviate in any substantial way from that of the U.S. Federal Reserve Board. Thus the trials and tribulations of Canadian monetary management are, to a certain extent, a reflection of success or failure in this area in the United States. One of the prominent features of the current period in North America, and particularly in Canada, is the re-emergence of a high positive real rate of interest.

Monetary policy, as dominated by the Federal Reserve Board on the North American continent since the 1930s, has been motivated by a number of objectives. Hindsight now tells us that, during the early stages of the Depression (from 1931 to 1938), monetary policy was extremely tight, even though nominal interest rates fell to almost zero. This was also a period of high real rates of interest. From 1938 to 1951, monetary policy accommodated the war effort, and the objective of the Federal Reserve was to ensure the orderly sale of the government debt. As a result, real rates fell and, during most of this period, were negative. It must be recalled that a system of rationing and price controls was in play during this period, brought on by the nature of the national emergency associated with the war effort. The period from 1951 to the early 1970s was also one of accommodation, with more ease having developed towards the end of that period. The Federal Reserve continued to focus on interest rate stabilization, with less concern being shown for the marketing of government securities. During this period, a positive real rate emerged, averaging between 1 and 2 percentage points – about equal to the then current rate of growth of total factor productivity.

In the 1960s pressures built up in international financial markets. These pressures came to a head in the early 1970s, when the U.S. Treasury announced its intention not to buy dollars in fixed relation to gold. Immediately, a new element was introduced into the conduct of monetary policy. For many countries, the decision had foreign-exchange implications for interest rates and interest-rate implications for the current account of the balance of payments. Real interest rates during this period turned negative.

In the mid-1970s these more fluid international financial markets – in combination with the persistence of inflation, among other things – led a rising number of central banks around the world to adopt growth targets for money supply and to focus less on interest rate stabilization. There was a strong belief among central bankers that the links between money supply growth and the rate of inflation were obvious. Too much new money implied higher rates of inflation. Inflation could be controlled by regulating the speed at which new money was created.

This short historical sketch of the way that central bankers pursued their objectives is instructive. At one time or another since the 1930s, central bankers have concentrated on three activities, either individually or as a group. These include: targeting of nominal interest rates; targeting of money supply growth rates; and/or exchange-rate stabilization activity. This broad perspective also suggests that the real rate of interest that emerges in pursuit of monetary objectives gives an important signal as to what "stance" that central bank has actually imposed on the economy. The impact that targeting of nominal interest rates and money supply growth rates, or exchange-market activity, has on real rates and the deviation of real rates from zero appears, in hindsight, to be a good indicator of the true stance of monetary policy – easy or tight.

With this in mind, the current high real rate of interest must then be taken as an indication that monetary policy on the North American continent in general – and in Canada in particular – is still tight relative to the 1951-71 period, and very tight relative to the 1972-74 period. The question is: Why? The obvious answer is, of course, that central bankers remain unconvinced that the expectation of inflation is no longer a threat and have adopted a stance that is consistent with that belief.

The current and prospective situation in the United States contains elements that could, if they are not held in check, give support to expectations of higher inflation and real rates of interest. The economic recovery in OECD countries and elsewhere could well see a reduction of foreign demand for U.S. securities, an adjustment to reduce the overvaluation of the U.S. dollar in foreign-exchange markets, and higher prices for imported goods and services. At the same time, the size and persistence of government deficits imply a continued increase in the size of the national debt in relation to GNP. In order to persuade lending institutions and the public to absorb the debt, higher U.S. government bond rates may be required. The U.S. government may find it hard to avoid the temptation to monetize a bit more than the usual share of the debt; in the longer run, this could inflate both nominal and real interest rates. The prospects, timing, and sequence of such developments are far from clear, however, given the difficulty in interpreting the monetary aggregates, the skittishness of confidence over government policies, and the uncertainties with respect to the expectations of asset holders.

What Can Fiscal and Monetary Policies Do?

If monetary policy errs on the side of tightness, with the underlying rate of inflation on the down trend, Canada could be drawn into a chronic period of high real interest rates, matched only by the period that followed the Depression in the 1930s and briefly revisited when real rates peaked in 1981-82. It would clearly be to Canada's advantage to explore every opportunity to keep real rates from rising. Directions in monetary policy that would ensure this result would be worth supporting, as would unilateral action by the Bank of Canada if U.S. monetary policy should follow a different path in light of the large federal deficits that must be financed in that country in the coming years. Such a position is not without its risks. A more relaxed domestic monetary policy, if pursued unilaterally, would produce additional real growth, but this would occur at the cost of a weaker Canadian dollar, which could put upward pressure on prices. In addition, an easier monetary policy, if it were too accommodating, could rekindle inflationary pressures directly.

What about fiscal policy? The April 1983 budget included $4.8 billion of federal programs to be initiated in 1983-84 to help spur the recovery. Also included were a number of special recovery taxes (increases in personal and indirect taxation). These new taxes will take effect in late 1984 and thereafter, once the economy has recovered. The base case projection indicates that many problems will remain after the 1983-85 period. In particular, the unemployment rate is not expected to fall below the double-digit level; a pause in real growth may occur after mid-decade; and the investment outlook remains unhealthy.

After adjusting for capital repayment costs and cyclical factors, a significant structural deficit is expected to remain in 1984. In the medium run, however, our assessment is that the federal budget will be near balance and that provincial budgets will be in surplus. Thus in the medium run there may be some need for adjustment.

The issue that is involved here is not only the appropriate mix of monetary and fiscal policy but also the timing associated with this mix. In light of the adjusted deficit results for 1983-84, it appears that enough fiscal stimulus is now present. With inflation possibly headed to below 5 per cent, however, continued adjustment of monetary policy will be necessary to ensure a balanced expansion of credit and to avoid any upward drift in real interest rates during the recovery period. In the medium run, the tax increases that are to take effect in 1984 and thereafter are necessary from the point of view of deficit reduction but less desirable from the point of view of sustaining recovery, since it appears likely that a balanced fiscal position can be achieved after an adjustment that includes these tax revenues. A policy of retaining the same taxing structure without considering further adjustments to fiscal policy might not be wise, especially if the recovery is not of the expected magnitude and strength.

What could the outcome be in the medium run if the tax rates and spending plans that are presently part of the government fiscal policy were altered? At the outset, we must recognize that general fiscal stimulus during the 1984-87 period would make only a minor dent in the unemployment problem. To

Table 3-14

Projected Impact of Fiscal Policy Initiatives,[1] 1984-87

	1984	1985	1986	1987
		(Per cent)		
Real GNE (1971$)				
Personal income tax cut	0.2	0.2	0.3	0.3
Corporate income tax cut	0.1	0.2	0.3	0.5
Manufacturers' sales tax cut	0.2	0.5	0.5	0.6
Increase in government expenditure	0.4	0.3	0.4	0.4
Consumer price index				
Personal income tax cut	--	--	0.1	0.1
Corporate income tax cut	--	-0.1	-0.1	-0.1
Manufacturers' sales tax cut	-0.9	-1.0	-1.1	-1.1
Increase in government expenditure	--	0.1	0.1	0.2
Unemployment rate				
Personal income tax cut	-0.1	-0.1	-0.1	-0.1
Corporate income tax cut	--	-0.1	-0.1	-0.2
Manufacturers' sales tax cut	0.1	-0.1	-0.1	-0.2
Increase in government expenditure	-0.2	-0.2	-0.3	-0.3
		($ Millions)		
Federal government balance				
Personal income tax cut	-723.2	-843.6	-907.7	-1,043.4
Corporate income tax cut	-709.1	-915.5	-1,119.1	-1,047.0
Manufacturers' sales tax cut	-1,022.9	-691.2	-689.0	-711.0
Increase in government expenditure	-510.6	-660.2	-715.9	-875.7
Current account balance				
Personal income tax cut	-298.0	-361.5	-529.9	-666.2
Corporate income tax cut	-90.3	-400.2	-575.3	-904.4
Manufacturers' sales tax cut	-234.2	-581.4	-403.2	-465.3
Increase in government expenditure	-362.2	-316.0	-464.4	-545.8

[1] These figures are deviations from the base case values.

SOURCE Economic Council of Canada, CANDIDE Model 2.0, 20 July 1983.

illustrate this, we consider a program of tax cuts about equal in size to the revenue gains expected from the taxes in the Special Recovery Program. For example, if tax cuts totaling between $3 and $4 billion (equal to the revenue gains of the special recovery tax) were introduced in 1984 and extended to 1987, cumulatively they would add between 3 and 4 percentage points only to the level of GNE and reduce unemployment by only 0.5 percentage points by 1987 (Table 3-14). Clearly, therefore, the unemployment problem must be dealt with at a different level.

The more immediate problem is to restore investor confidence and to retain the recent gains made in restoring consumer confidence. This, of course, is related not only to the firmness of government policy but also to its consistency and continuity. Finessing strong and balanced medium-run growth from a recovery that lacks a proper restoration of investor confidence would be difficult. Monetary or fiscal policy cannot play the role of a cure-all, but it can make a modest contribution. What is necessary is a much wider range of policy initiatives that treat chronic problems directly.

4 Social Concerns

As we observed in Chapter 1, the increase in average real personal incomes over the past 20 years has been substantial. The concept of economic well-being in a society goes beyond mere averages, however, to consider the fate of those persons who are the most vulnerable to the economic and social transformations inherent in the growth process. The policy recommendations made in this Council's Fifth Annual Review, for example, reflected the finding that many of Canada's poor participate in the labour force, albeit marginally.[1] In the 15 years since that report was published, there have been major demographic and institutional changes, such as the increase in the labour force participation of women and the manifold experiments in employment, retraining, unemployment insurance, and housing programs, all of which have had an impact on the income and security of families. Higher levels of divorce and the breaking-up of family units, on the other hand, have tended to unravel family-based income support systems and to place more individuals "at risk." The recession, along with the accompanying deterioration in labour market conditions, has cut into the earnings of many Canadians and, through shortfalls in revenue growth, has constrained the ability of governments to intervene on their behalf Here, we examine some aspects of the traditional "safety nets" in the light of these developments.

In Chapter 3 we noted a deterioration in the capacity of the economy to employ those wanting to work. Unemployment is not expected to decline, over the entire projection period, to even the rates experienced during the late 1970s (between 7.5 and 8.5 per cent), or to less than 1 million jobless Canadians. The pressures that the social security system has endured over the past two years cannot, therefore, be expected to evaporate rapidly.

As indicated in Chapter 1, unemployment insurance, social assistance, and other programs aimed at countering human deprivation and encouraging employment entail large-scale government expenditures in Canada and in almost all of the other OECD nations. With the deterioration of economic performance leading to high levels of inflation and unemployment, these programs have exerted immense expenditure pressures, involving serious costs and economic distortions. We are therefore mindful that, however worthy their objectives, they are at best imperfect substitutes for a healthy economy in which private saving, spending, and investment initiatives provide most of the jobs and incomes for Canadians. As more and more resources are taken up by them, there is the danger that the inherent distortions and dependencies that they create will impede the economic recovery and the high levels of productivity, employment, and income growth that we all seek. It is in this context, with an eye to reducing the inefficiencies that exist, that we approach "safety net" issues.

Economic security hinges, in the main, on attachment to the labour force. The provision of security in a complex society is correspondingly complex, however, and our review of the relevant programs reflects this fact. While the unemployment insurance system has been expanded over the years, it is still no monolith. In those cases where other social security programs are inoperative, Canadians remain dependent on the welfare programs that are run on a cost-sharing basis under the Canada Assistance Plan. Therefore, to see how the various programs are woven into an adequate safety net and, particularly, how the most vulnerable persons in society are faring, we must go beyond the first line of defence and examine some of the income support programs themselves. We can then examine how persons in a variety of family and labour force situations are affected by the interplay of a range of cash transfer programs, and we can compare the results with those in some other western countries, where rather different approaches have been followed in devising social security systems. In addition to cash transfers, of course, there are programs of tied aid that sustain living standards such as medical care, daycare, and education. Later in this chapter, we focus on one such area – the provision of adequate shelter for those in need.

Traditionally, the impact of economic setbacks on individuals was cushioned by family networks. In Canada as elsewhere, however, the number of households comprised of only one adult has been increasing steadily, and most such persons can no longer rely on financial support from blood relatives. Confining our attention to situations where the head of the family is under 65 years of age, persons not in families and single-parent families together rose from 33 per cent of all family units in 1971 to 38 per cent in 1979. On the other hand, there has been a dramatic increase in the number of multiple-earner families, in keeping with the rising participation of women in the labour force, which has given those families substantial protection against extreme drops in income. Whereas only 43 per cent of husband-and-wife families reported that both spouses were in the labour force in 1971, 60 per cent were in that category in 1979 (Table 4-1). Of the husband-and-wife families in which the husband experienced unemployment in 1979, the wife worked in over half of the cases, as opposed to only one-third in 1971. This perspective is further corroborated by a 1982 survey of persons who had exhausted their unemployment insurance benefits, which showed that 63 per cent belonged to families in which at least one other member was employed.[2]

Table 4-1

Distribution of Husband-and-Wife Census Families[1] (with the Husband Aged Less than 65), by Employment and Unemployment Characteristics,[2] Canada, 1971 and 1979

	1971	1979
	(Per cent)	
Employment:		
Husband only worked	53.7	36.5
Wife only worked	0.9	1.4
Both husband and wife worked	42.7	59.2
Neither husband nor wife worked	2.7	2.9
Total	100.0	100.0
Unemployment:		
Husband only had unemployment spells	11.3	10.1
Wife worked	3.8	5.3
Wife did not work	7.4	4.8
Wife only had unemployment spells	5.3	7.7
Husband worked	5.1	7.5
Husband did not work	0.2	0.2
Both husband and wife had unemployment spells	1.8	2.4

1 A census family consists of the husband, wife, and any unmarried children residing with them or one parent and any unmarried children.

2 Characteristics of the husband and wife only. Those who did not work showed no recorded employment during the entire year.

SOURCE Statistics Canada, Survey of Consumer Finances, special tabulations.

The Unemployment Insurance Safety Net

The recession from which we are emerging hit many persons who had previously enjoyed relative job security. This, in turn, contributed to a dramatic escalation of unemployment insurance expenditures by increasing both the number of claimants and the average benefits paid to them. From 1981 to 1982, when the average monthly unemployment count grew by 45 per cent, the average monthly number of UI benefit recipients climbed by 57 per cent (from 720,000 to 1,138,000). The total amount of benefits paid out rose even more rapidly by 78 per cent (from $4.8 billion to $8.6 billion).[3] Part of this increase can be attributed to certain features of the system.

The program is designed, for example, so that the criteria determining both the eligibility for benefits and their duration can respond to changes in economic conditions. To receive benefits, the unemployed worker must have been in an insurable job for a minimum number of weeks during the 52-week reference period preceding the application for benefits; this number can vary from 10 to 14 weeks, depending on the regional unemployment rate.[4] In August 1981, just before the jump in unemployment rates, only about half of Canada's 55 UI regions required only the minimum of 10 weeks of eligible prior employment; by February 1983 virtually all of the regions had set that minimum. As for the duration of benefits, extension beyond the basic entitlement period also depends on the regional unemployment rate, with two additional weeks of benefits being granted for each increment of 0.5 percentage point in the regional unemployment rate above 4 per cent, to a maximum of 32 weeks. In August 1981 about one-quarter of the regions allowed the maximum extension, but this proportion had climbed to three-quarters by February 1983. This increased access to benefits confirms both the severe deterioration of labour market conditions and the capacity of the social security system to absorb some of the adverse consequences.

By affecting groups that normally have low rates of unemployment and thus changing the composition of the recipient population, the recession has led to higher UI payments. Over the past two years, unemployment has deeply affected adults (especially men) of prime age (Table 4-2) who previously had stable, well-paid jobs. Since earnings are relatively high at that career stage, the shift has tended to raise the average weekly UI payments (Table 4-3). In 1983 more beneficiaries had insurable earnings above the ceiling than in 1981, and more of them had spent the entire qualifying period in insurable employment (50 to 52 weeks preceding the claim for UI benefits) than had been the case two years earlier (Table 4-4). As a result, larger numbers of unemployed are now drawing benefits for longer periods of time; in July 1982, for instance, over 300,000 had been receiving regular benefits continuously for more than six months – roughly twice as many as one year before.

Table 4-2

Unemployment Insurance Beneficiaries[1] in January, by Age and Sex, Canada, 1981-83

	January 1981		January 1982			January 1983		
	Number	Distribution	Number	D'stribution	Increase over 1981	Number	Distribution	Increase over 1982
		(Per cent)		(Per cent)	(Per cent)		(Per cent)	(Per cent)
Both sexes	759,978	100.0	959,344	100.0	26.2	1,367,879	100.0	42.6
Men								
Under 20	46,433	6.1	57,051	5.9	22.9	65,969	4.8	15.6
20-24	114,723	15.1	151,803	15.8	32.3	208,884	15.3	37.6
25-34	142,494	18.7	185,618	19.3	30.3	280,480	20.5	51.1
35-44	76,239	10.0	95,307	9.9	25.0	147,857	10.8	55.1
45-54	62,962	8.3	75,216	7.8	19.5	108,467	7.9	44.2
55-64	50,610	6.7	58,509	6.1	15.6	85,917	6.3	46.8
Total	493,461	64.9	623,504	65.0	26.4	897,574	65.6	44.0
Women								
Under 20	21,935	2.9	26,824	2.8	22.3	34,782	2.5	29.7
20-24	63,153	8.3	78,880	8.2	24.9	110,456	8.1	40.0
25-34	80,621	10.6	103,502	10.8	28.4	145,881	10.7	40.9
35-44	46,999	6.2	61,390	6.4	30.6	88,217	6.4	43.7
45-54	34,175	4.5	41,964	4.4	22.8	57,821	4.2	37.8
55-64	19,634	2.6	23,280	2.4	18.6	33,148	2.4	42.4
Total	266,517	35.1	335,840	35.0	26.0	470,305	34.4	40.0

[1] Here, beneficiaries are only the regular benefit recipients.

SOURCE Based on data from Statistics Canada.

Table 4-3

Average Weekly Insurable Earnings in January of Beneficiaries Receiving Regular UI Benefits with No Earnings Reported, by Sex, Canada, 1981-83

		January 1982		January 1983[1]	
	January 1981	Amount	Increase over 1981	Amount	Increase over 1982
	(Dollars)	(Dollars)	(Per cent)	(Dollars)	(Per cent)
Both sexes	221	241	9.0	264	9.5
Men	242	264	9.1	290	9.8
Women	181	196	8.3	212	8.2
Ceiling	315	350	11.1	385	10.0

[1] Preliminary figures.

SOURCE Based on data from Statistics Canada.

Table 4-4

Distribution of Beneficiaries Receiving Regular UI Benefits in January, by Weeks of Insurable Employment,[1] Canada, 1981-83

	January 1981		January 1982		January 1983[2]	
	Number	Distribution	Number	Distribution	Number	Distribution
		(Per cent)		(Per cent)		(Per cent)
Under 15 weeks	55,867	7.4	59,564	6.2	116,649	8.5
15-19 weeks	65,854	8.7	73,061	7.6	99,595	7.3
20-29 weeks	242,695	31.9	297,835	31.0	360,299	26.3
30-39 weeks	142,209	18.7	179,492	18.7	221,483	16.2
40-49 weeks	130,789	17.2	171,916	17.9	245,793	18.0
50-52 weeks	122,564	16.1	177,476	18.5	324,060	23.7
Total	759,978	100.0	959,344	100.0	1,367,879	100.0

[1] The duration of insurable employment is the number of weeks of employment during which UI premiums have been paid during the 52-week period preceding the application for benefits.

[2] Preliminary figures.

SOURCE Based on data from Statistics Canada.

Labour Market Policy

The Past Record

Canada has a long history of activity in the area of manpower policy. Even in the 1930s, specific programs were implemented to alleviate the worst effects of the Depression. More recently, over the period of existence of this Council, governments have been active in the labour market as part of their commitment to "full" employment. Among the OECD countries, Canada (together with Sweden) has for many years recorded the highest proportions of expenditures on manpower policies relative to GNP. These policies have been adapted to the changing labour market conditions but also to the way that other macroeconomic policies have been used. Indeed, throughout most of the 1960s public policy relied mainly on aggregate demand measures (monetary and fiscal policies) to solve labour market problems. In late 1960s and early 1970s it became obvious that those policies could not eradicate specific unemployment problems in particular regions or within specific demographic groups without creating unbearable inflationary pressures. This explains the rapid development of appropriate legislation in different areas – the Adult Occupational Training Act (AOTA) in 1967, the creation of the Department of Regional Economic Expansion (DREE) and the introduction of regional economic incentives in 1968, the changes in the Unemployment Insurance Act in 1971, and the emergence of experimental job creation schemes such as the Local Initiatives Program (LIP) and Opportunities for Youth (OFY), also in the early 1970s. Programs of these types still constitute the basis of manpower policy today, at least in terms of some of their orientations.

Over time, the objectives of training policy have been altered. At its inception, the main objective of the AOTA program was the development of a productive labour force, with emphasis being placed on relatively general skills that would enhance the nation's economic prosperity. But as structural unemployment took on greater significance, the purpose of the program shifted towards a better matching of specific occupational skills with the new job requirements that were emerging. In 1982 the federal government enacted the National Training Plan, whose objective is focused deliberately on the needs of the labour market; elaborate provisions were made for obtaining and forecasting information on future job requirements and for delivering that information and the appropriate training funds to the provinces. It is too early to evaluate the effectiveness of the program, especially since the recession has obscured the potential skill shortages in the labour market.

The other main focus of manpower policy has been job creation. Innovative efforts in this direction have included LIP and OFY, both created in 1971, and the Local Employment Assistance Program (LEAP), which was established in 1973; other schemes followed, most of which were consolidated into the

Canada Works program, introduced in 1977. Many of these programs were, in one way or another, aimed at creating temporary jobs for specific groups in the public or quasi-public (community-based) sector. Emphasis was given to regions with historically high records of unemployment. After several years of experimenting with such measures, however, misgivings were expressed about the effectiveness of some of them. These doubts may have spurred government towards programs of wage subsidies to the private sector. One such scheme – the Employment Tax Credit Program – was implemented in 1978 and remained in effect until March 1981. It was a partial success: about 120,000 jobs were created over the three-year period. But the program was designed in such a way that it failed to reach the very large number of small businesses that pay little or no taxes, many of which can expand their work force quite quickly.

Recent Initiatives

This, then, was the setting when the recession shook the economy to its foundations. Without doubt the unemployment insurance system served as the main line of defence throughout the recession. Although it was initially preoccupied mainly by the fight against inflation, the federal government, in the face of rising unemployment rates, revived two programs in December 1981 – a work-sharing program and a job creation program, under Section 38 of the Unemployment Insurance Act – the costs of which were charged to the UI fund, because of an overriding concern about the growing overall federal deficit. Faced with worsening economic conditions, a growing number of unemployed, and pressures to act to alleviate the financial burden of those who had exhausted their entitlements to UI benefits, the federal government then introduced the first sizable increase in public funds allocated to job creation in the fall of 1982, in the form of the New Employment Expansion and Development (NEED) program, funded from general revenue. More recently, as part of the measures accompanying the April 1983 budget, the Minister of Employment and Immigration announced a reshaping of the labour market strategy for the 1980s, with consolidation and revamping of the job creation programs to take place this autumn.

UI-Based Work-Sharing Program

By reducing the number of hours worked, the work-sharing program was originally designed as an experimental alternative to the layoffs caused by temporary production cutbacks. In a firm with 100 employees, for example, a 20 per cent reduction in staff hours for all employees in response to a similar drop in production would avoid the layoff of 20 people. The UI benefits would then provide partial compensation (60 per cent) for the wages lost. This approach would lower the individual cost of the decline in the workload but would not increase the cost to society – in theory, at least.

First introduced on a trial basis, with less than favourable evaluations and little support from labour unions, the work-sharing program was intended as a six-month stopgap alternative to massive cyclical layoffs. It was later extended, however, and its funding was increased substantially. At the same time, there was greater effort to confine the application of the program to those cases where drops in output are genuinely temporary. The response was immediate and extensive: after only three months, nearly 500 applications (covering over 26,000 workers) had been approved, and close to 12,000 layoffs had been avoided. By March 1983 about 12,000 applications had been approved, covering 242,000 workers and over 100,000 potential layoffs.[5]

Although the program has limited application, these figures are an impressive indication of the willingness of people to close ranks in order to resolve temporary crises, especially when they are supported by UI entitlements. Overall, though, the cost of work sharing to the unemployment insurance system is about 1.5 times greater than that of the benefits paid out during layoffs, primarily because the participating workers retain full eligibility to benefits, because there is no waiting period, and because there are differences in average wages between those who share work and those who would have been laid off. By simply delaying layoffs – a frequent occurrence in a prolonged recession – work sharing triggers an accumulation of costs rather than a substitution. In fact, about half the jobs saved by a work-sharing agreement have been subject to layoff either immediately or shortly after the termination of the agreement.

Employment and Immigration Canada has described the work-sharing program as central to the process of cyclical or seasonal adjustments – "a true alternative solution to lay-offs."[6] While we recognize the difficulties in adapting this approach to some types of operations, we believe that, as a permanent part of the employment program arsenal, work sharing can be a useful voluntary supplement in responding to society's needs. But its financing should be examined in the context of other measures to create or preserve jobs.

UI-Based Job Creation Programs

During the late 1970s, as an adjunct to the unemployment insurance system, there was experimental use of UI funds to finance job creation projects aimed at employing beneficiaries. Subsequently, a Task Force on Unemployment Insurance evaluated the program and concluded that it offered "no evidence . . . to demonstrate the impact on the employability of the people involved in the projects," for several reasons: a) the projects were costly because an amendment to UI regulations permitted payment of benefits that were much higher than under normal circumstances, in order to interest recipients in participating in the program; b) employment-related costs also had to be paid; it was impossible to determine whether the projects were successful in generating positive effects for the communities involved or for the employability of the participants; c) there were doubts about the strategy implicit in this approach.[7] The Task Force added: "In terms of UI's role in the labour market, a basic inconsistency may exist when benefits are paid to persons while they work. This is true if time spent on temporary job creation projects is likely to prevent them from looking for longer term, more stable employment."[8] Nevertheless, with the onslaught of the recession the federal government again decided, as noted above, to allocate UI funds to job creation projects, in accordance with Section 38 of the Act. By the end of April 1983 about 30,000 persons were participating in this program.

NEED and Canada Works

Introduced in October 1982 to cope with the increasing number of people who were running out of UI entitlements, the NEED program was developed in cooperation with the provinces and territories and with the private sector (including nonprofit organizations). It was aimed at the creation of productive jobs for UI exhaustees and welfare recipients. The federal government allocated $500 million to create temporary jobs between November 1982 and March 1984, and the provinces (except Quebec) responded with contributions of their own (totalling $152 million to date) to support this effort.[9] The private sector also reacted positively. Employment and Immigration Canada recently reported that 85,000 to 90,000 jobs are expected to have been created before the termination of the program, with the average job duration being 23 weeks.[10]

Total expenditures in job creation programs (including NEED) reached a high in 1982-83, at about $600 million; and more than 200,000 persons participated in the programs (Table 4-5). The consolidation of job creation programs, announced in April 1983, will be labeled Canada Works and will give birth to a new NEED program that will replace the 1982 scheme and incorporate other federal employment-related programs. Its stated objective is to provide jobs through a wide range of projects of lasting value to the community. Particular encouragement will be given to participation by the private sector, since it has the capabilities for providing long-term employment. To start with, the new program will be allocated $380 million this autumn. The target

Table 4-5

Job Creation and Training Programs: Numbers of Participants and Costs, Canada, 1977-83

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83[1]
Job creation programs[2]						
				(Thousands)		
Participants	113.4	99.6	128.4	131.9	78.6	215.1
				($ Millions)		
Expenditures	410.6	276.4	281.3	256.1	277.9	608.8
Canada Manpower Training Program (CMTP)						
				(Thousands)		
Trainees	299.4	266.5	225.7	315.6	292.6	271.8
				($ Millions)		
Expenditures[3]	572.2	637.3	532.2	762.5	829.8	919.7

1 Preliminary figures.

2 The Employment Tax Credit Program was in effect from 1978-79 to 1980-81. Since it was not an expenditure as such, it is not included in the expenditures, but the number of participants takes the program into account.

3 Including expenditures under Section 38 of the Unemployment Insurance Act.

SOURCE Employment and Immigration Canada, *Annual Reports*, various years.

population is much larger than that of the previous program: it includes laid-off workers, UI exhaustees, UI recipients, social assistance recipients, returning students, and members of those communities and industries designated by the Industrial and Labour Adjustment Program (ILAP) as experiencing high levels of unemployment caused by large-scale industrial change.

The new NEED program will be one of four components of the consolidated job creation package. The other three components and their objectives are described as follows:

- The Access program, through wage subsidies, helps to provide employment experience in the private sector for people who have difficulty entering the permanent labour market;
- The Job Corps program assists disadvantaged workers to develop the skills and work habits that they need to become productive members of the regular labour force;
- The Local Employment Assistance and Development (LEAD) program supports long-term, community-based planning and employment development in slow-growth regions and in communities where chronic high unemployment persists.

In its recent report on the labour market, this Council recommended the implementation of job creation programs directed at the private sector.[11] Our analysis of private sector programs suggested that they are likely to have certain advantages over programs of public employment (which are more traditional in Canada) in terms of cost effectiveness and employment stability. After the successful cooperation with the private sector achieved by the NEED program, the government is gearing its other programs in that direction.

The overall envelope for job creation should amount to $1.6 billion, to be spent over the two fiscal years 1983/84 and 1984/85. But, in terms of expenditures, the unemployment insurance system bore the heaviest burden during the recession because of the increased regular payments and because of the funding of the work-sharing and job-creation initiatives. While the growth of UI expenditures gives an exaggerated impression of the responsiveness of federal employment-related programs overall, it was perhaps inevitable that the huge rise in unemployment and the spectre of UI exhaustion would prompt considerable restructuring and reorientation of programs. The prospect of continuing high unemployment rates will likely prolong this costly process, and if the new programs are to become permanent features, their operation from the standpoints of efficient labour allocation and appropriate method of financing will take on added importance.

Despite the easing of qualification criteria and the expansion of job-creation, work-sharing, and training programs, the capacity to protect people through the unemployment insurance system is limited. At the end of 1982 the number of UI exhaustees was more than 75 per cent higher than a year earlier. In addition, there were growing numbers of persons who could not get enough work to qualify for UI benefits and of discouraged workers who had no hope of landing a job because so many were competing for work. Some of these people had no recourse but to turn to social assistance.

Social Assistance

If our projections in Chapter 3 have any substance and if unemployment is to remain at double-digit levels throughout most of the 1980s, there will be much greater pressure on the capacity of Canada's present welfare system to help those most severely affected by poor labour market conditions. This could represent a major departure from the 1970s, when the number of multiple-earner families increased and the unemployment insurance system expanded, so that welfare tended to play a limited role in providing income maintenance for most persons who were actively seeking work. At that time, most employable people relied on welfare for quite short periods of time, although renewals were not uncommon. This is illustrated by the turnover statistics for the municipality of metropolitan Toronto. An employable person who was put on active welfare, say, in November 1980 had a 29 per cent chance of being off welfare in one month's time and only a 10 per cent chance of still being on welfare one year later (Table 4-6). In the past, therefore, for most applicants who were able to work, welfare was not used as a substitute or an alternative for work but, rather, as a temporary income support.

Most of the time, the number of employable persons on welfare was quite low in relation to both the total welfare caseload and unemployment. According to a report prepared for the Interprovincial Conference of Ministers Responsible for Social Services, in 1977-78 less than 30 per cent of the total monthly caseloads in Canada comprised unemployed persons who were considered by welfare authorities to be employable, and another 4 per cent consisted of persons working full-time or part-time. During the same period Statistics Canada reported that close to 800,000 households had one or more unemployed members (including nearly 350,000 with an unemployed head) – well above the estimated average monthly number (180,000) of unemployed but employable welfare cases.[12]

Table 4-6

Approximate Retention Schedule for Employable General Welfare Assistance Cases, Metropolitan Toronto[1]

	Cases retained on active G.W.A.
	(Per cent)
Duration of retention (months):	
1	71
2	40
3	29
4	24
5	21
6	18
7	16
8	15
9	14
10	13
11	12
12	10

[1] Calculated in 1982.

Source Social Services Division of the Department of Community Services, Municipality of Metropolitan Toronto.

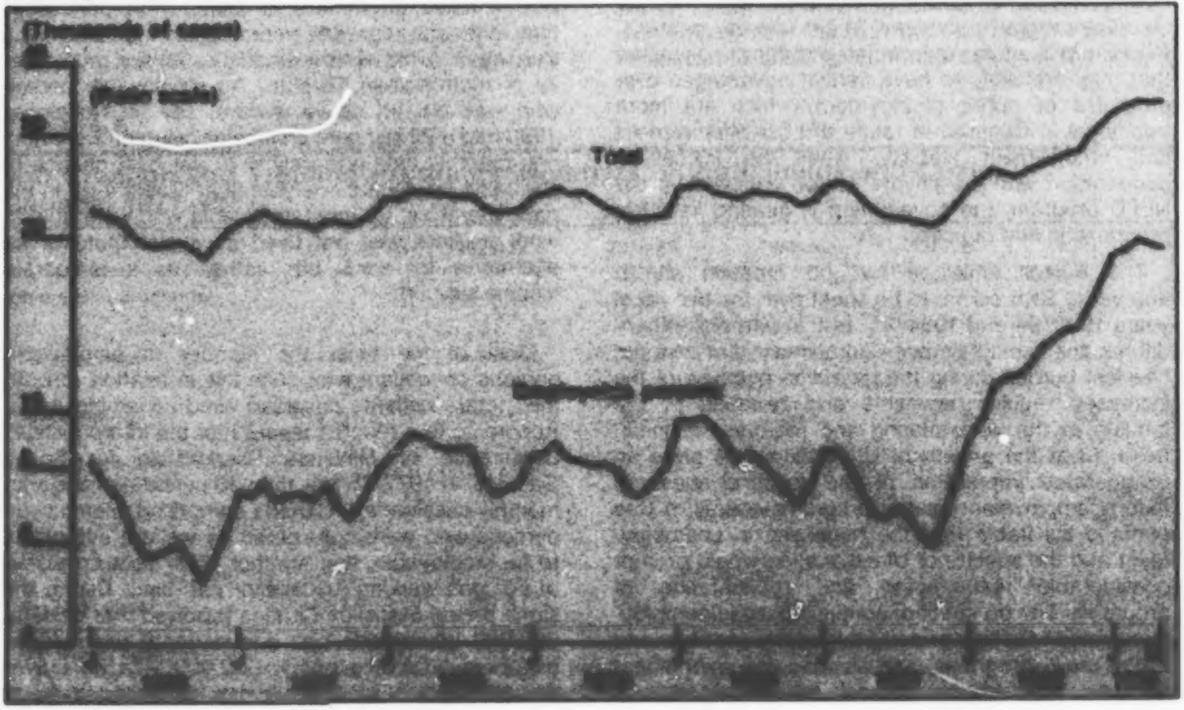
Recent Caseload Increases

With the recession, the need for welfare associated with temporary unemployment rose again recently. According to a survey by Employment and Immigration Canada, of the unemployed who, in July 1982, had exhausted their UI benefits during the previous month, 10 per cent had to turn to welfare.[13] Not surprisingly, the increase in the total number of welfare cases lagged behind that of the unemployed during the recession, just as did the exhaustee count since, among the exhaustees, many drew first upon other savings. But there is evidence that the number of families in financial difficulty is growing.

This is highlighted by the figures for metropolitan Toronto. After years of very contained fluctuations in the total caseload, a persistent upward trend began late in 1981 (Chart 4-1). By November 1982 the caseload was 38 per cent higher than a year before; the number of employable persons, which had declined somewhat in 1980 and 1981, had risen dramatically by 140 per cent. There had been substantial increases in the numbers of single

Chart 4-1

Metropolitan Toronto General Welfare Assistance Caseload, January 1976–May 1983



Source Municipality of Metropolitan Toronto.

employable persons, both male and female, and the number of employable male family heads had almost doubled (Table 4-7). The Toronto welfare caseload has leveled off in recent months, but at a much higher number than during the 1976-80 period and with a much larger proportion of employable cases.

Table 4-7

Distribution of General Welfare Assistance Caseload in November, Metropolitan Toronto, 1980-82

	1980	1981	1982
		(Per cent)	
Employable persons	30.8	30.4	52.9
Male family head	6.8	6.3	9.2
Female family head	3.7	3.6	12.4
Single men	14.2	15.1	23.4
Single women	6.0	5.3	7.9
Unemployable persons	69.2	69.6	47.1
Male family head	6.9	7.1	5.7
Female family head	17.1	16.0	4.6
Single men	24.3	24.9	19.8
Single women	20.1	21.0	16.4
Foster children	0.7	0.6	0.5
Total	100.0	100.0	100.0
Number of cases	22,534	21,753	29,980
Number of beneficiaries	37,602	35,416	48,390

SOURCE Based on data from the Social Services Division of the Department of Community Services, Municipality of Metropolitan Toronto.

Although such increases were pervasive throughout Canada, the available caseload statistics indicate considerable variation between the provinces in the extent to which welfare programs expanded during the recession. Some of this is due to differences in the regional impact of the downturn, to the availability of other social security programs (such as fishermen's unemployment insurance benefits in the Atlantic region), and to provincial social assistance policies.[14] New Brunswick, for example, perhaps because it already had a high welfare take-up rate and because cases of emergency assistance are excluded from the count, experienced a relatively small increase in caseload (Chart 4-2). Quebec, with a welfare dependency rate that has traditionally been above the national average, reported moderate increases during the earlier stages of the recession; but late in 1982 rapid growth occurred, with the increase in the number of single, relatively young persons being especially large. The fading economic boom in Alberta contributed to rapid growth in that province's caseload throughout most of 1982 and 1983 – by 38 per cent in the twelve months to March 1983. Cases of employable men with dependants increased markedly during this period.

Program Changes

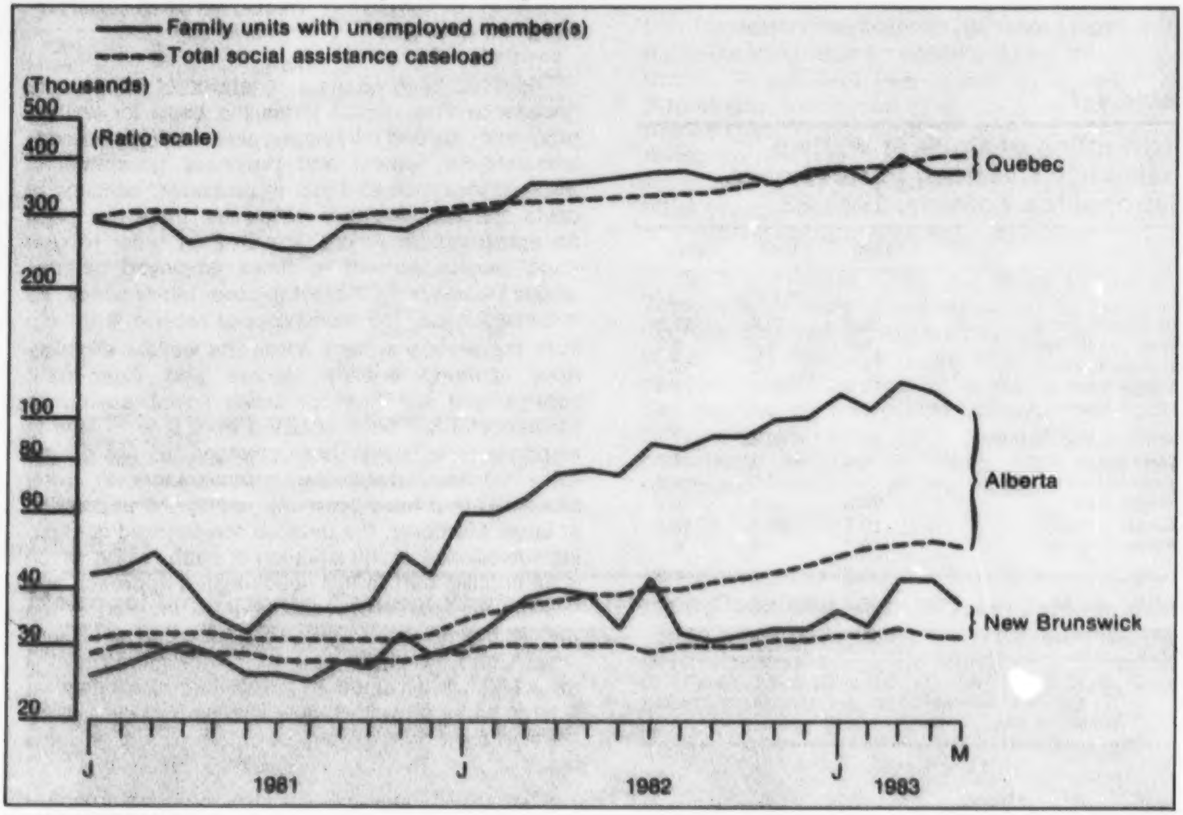
There has been no major extension of the Canada Assistance Plan, which forms the basis for welfare programs funded through cost-sharing accords between the federal and provincial governments, since its inception in 1966. In particular, because of costs and administrative difficulties, there has been no agreement to amend the CAP in order to give more income support to those employed persons whose income is insufficient to cover family needs. As a consequence, the working poor receive little help from the welfare system. While the welfare eligibility rules covering outside income and liquid-asset ceilings and the level of basic social assistance allowances have been adjusted from time to time in response to inflation, these changes did not necessarily correspond to the improvements in living standards that have been enjoyed by the population at large. Moreover, the detailed scrutiny and continuing surveillance of the situation of each family, which is an intrinsic part of this needs-tested approach and has been a source of resentment on the part of the people concerned, is probably accepted even less widely today. In short, at a time when more persons have been thrust upon it, the welfare alternative, at least in some provinces, may well be a more desperate last resort than it ever was before.

Since 1975, in particular, the program changes made in some provinces have tended to reduce the system's role in maintaining the income of the unemployed. Regulations have made it harder for the latter to stay on welfare or have reduced their allowance relative to that of other recipients. At the same time, some programs have been introduced to increase the employability of those clients who participated and to reduce the financial costs and risks faced by those who are trying to move off welfare into employment.

During the height of its economic boom, Alberta took a particularly aggressive approach in this regard. In 1978 it reclassified many single parents as "employable," thereby requiring them to seek work and to justify any job refusals before being eligible for welfare benefits. Simultaneously, the length of time that single employable persons could remain on welfare was limited to two weeks, with a possible extension of another two weeks. In 1979 Alberta also stipulated that, except in special circumstances, the

Chart 4-2

Family Units Experiencing Unemployment and the Social-Assistance Caseload, Selected Provinces, January 1981–May 1983[1]



1 Unadjusted data.

SOURCE Based on data from Statistics Canada, the New Brunswick Department of Social Services, Quebec Ministry of Social Affairs, and the Alberta Ministry of Social Services and Community Health.

spouses of social assistance clients were expected to seek employment. The province's Employment Opportunities Program offered assessment, employment preparation, counseling, placement, and follow-up services in order to improve the clients' chances of finding employment. Rehabilitation services and money to cover certain job-finding expenses were also provided. In its report for 1979-80, the Alberta Ministry of Social Services and Community Health noted a substantial decline in the number of cases classified as single-parent or employable, attributing this development in part to those policy changes. Although the recession subsequently prompted some relaxation of welfare regulations pertaining to employable persons, differential treatment on the basis of "reason for need" persists as a feature of this and many other programs.[15]

The Welfare-to-Work Transition

When only low-wage jobs are available for families with several dependants, full-time work may yield even less disposable income than complete reliance on welfare. Programs to increase the incomes of families with marginal job opportunities, because of the constraints on CAP, have been developed by individual governments, so that there is even greater variability in these programs across Canada than in the welfare system itself. Income tax credits, such as the federal child tax credit and various provincial property/rent tax credits, provide extra income. Saskatchewan, Quebec, and Manitoba have experimented with cash transfer programs that straddle the welfare-to-work transition; yet, like the tax credit, they neither confine assistance to welfare recipients nor involve close personal surveillance. All three schemes link payments to the amount of family income and the number of children, but Quebec's program also contains a direct work incentive because the amount of the transfer is determined by the level of earned income, and it rises (within a defined range) as the latter increases. Aggregate expenditures under all three income-supplement programs are small, partly because of the apparently low rate of take-up by those who are eligible for benefits.

A study prepared for the Canadian Institute for Economic Policy calculated that, among families with several dependants and very low earnings (e.g., a two-parent, two-child unit with one member working full-time) in 1979, taking into account taxes, social security deductions, and income transfers, only in Saskatchewan, Quebec, and Ontario was a family better off if the head worked at the minimum wage for a full year rather than depend on welfare.[16] Even in Quebec, where the net income advantage from working was estimated to be the highest, total reliance on social assistance provided an income that was equivalent to over three-quarters the amount that would have been obtained had the family head worked. While the income-supplement and tax-credit programs have been extended since 1979, the Institute's study clearly shows that the social security system still faces major problems in achieving a reasonable balance, with respect to minimum income, between those who have access to employment and those who do not. It is also apparent that the problem is not due to the excessive generosity of welfare benefits (Table 4-8). A family head attempting to attain a better livelihood by combining welfare payments and earnings from work is confronted by high tax-back rates as social assistance is reduced (above the exemption level), sometimes on a dollar-for-dollar basis.[17] This problem of work disincentive is caused in part by the way the social security system has developed in Canada. We shall return to this issue later.

In summary, the combination of greater labour force participation by spouses, retraining and job creation programs, UI benefits, and social assistance has generally provided a relatively viable – but by no means excessive – income-support safety net in these hard economic times. The costs, personal disillusion, inefficiencies, and opportunities forgone have been heavy, however. Given the depth of the recession, the lack of jobs, and the increase in the number of those who have exhausted their UI benefits, inevitably there have been increases in the welfare rolls, particularly of unemployed but employ-

Table 4-8

Disposable Income[1] for a Family of Four, by Work Status and by Province, Canada, 1979-80

		Family head works full-time			Statistics Canada low-income cutoffs, by area of residence	
	Family is on social assistance[2]	Annual minimum wage income[3]	Net supplementary income[4]	Total disposable income	Urban, population 500,000 or over	Rural
			(Dollars)			
Newfoundland	7,200	5,800	700	6,500	11,627	8,454
Prince Edward Island	6,900	5,700	700	6,400	11,627	8,454
New Brunswick	6,700	5,800	700	6,500	11,627	8,454
Nova Scotia	6,400	5,700	700	6,400	11,627	8,454
Quebec	7,200	7,200	1,800	9,000	11,627	8,454
Ontario	6,900	6,200	1,000	7,200	11,627	8,454
Manitoba	8,000	6,300	1,200	7,500	11,627	8,454
Saskatchewan	6,700	7,300	1,500	8,800	11,627	8,454
Alberta	10,500	6,200	800	7,000	11,627	8,454
British Columbia	9,100	6,200	800	7,000	11,627	8,454

1 Rounded to the nearest hundred.
2 Social assistance, or welfare, is the level of assistance available for a family of four with "average" needs, plus provincial and federal family allowances and the child tax credit, all calculated at the beginning of 1980. A family of four is made up of two adults and two children.
3 Annual minimum wage income is equivalent to the provincial minimum wage as at 31 December 1979, multiplied by 52 working weeks of 40 hours each.
4 Net supplementary income is the net cash supplement available from all sources in 1979 at the particular annual minimum wage income (benefits minus taxes and premiums).

SOURCE D. P. Ross, *The Working Poor: Wage Earners and the Failure of Income Security Policies* (Ottawa: Canadian Institute for Economic Policy, 1981); Statistics Canada, *Income Distributions by Size in Canada, 1979*, Cat. No. 13-207, 1979.

able persons. While the federal and provincial job creation schemes are helping to contain the pressure, welfare has probably become a more important source of income maintenance for able-bodied Canadians during this protracted period of high unemployment. But welfare programs are not ideally designed for this purpose. Typically, the treatment of employable persons is based on the assumption that there are employment opportunities available, albeit often temporary and poorly paid. And, as yet, within the system's needs-tested framework, there are insufficient opportunities for betterment through paid employment for persons with limited earning potential and with dependants to support.

An International Comparison

Very few families receive the "average income." Most, regardless of the type to which they belong, find themselves higher or lower than the average in the income spectrum. Where they are in the scale is likely to reflect many factors, including the work record of individual family members and the impact of many elements found in the federal and provincial systems of taxation and transfer payments. Overall, taxes and transfers affect incomes in two distinct ways: directly, by paying benefits or imposing taxes; and, indirectly, by encouraging or discouraging gainful employment or other activities that influence incomes.

The questions of how taxes and transfers affect the income situation of different types of families and how various national systems rank were recently investigated in an international study in which this Council participated.[18] The countries studied were Australia, Canada, West Germany, France, Israel, Sweden, the United Kingdom, and the United States.

The study was concerned with how generously the governments of these countries were responding to the economic needs of families with children, and thus it excluded the retired and the elderly. It concentrated on how different types of families fared with regard to yearly income, both within and between countries, as well as on the alternative approaches to income transfers used by the countries examined. For purposes of comparison, family types were chosen according to composition (number of children), structure (one- or two-parent families), labour market behaviour, and wage levels (relative to the average going wage).

The international comparisons were limited to direct cash transfers and taxes. A host of elements were thus excluded from what most would consider to be a complete picture of family well-being – housing or rent subsidies, education, medical care, personal social services, and employment programs, among others. A more complete picture would also include fringe benefits from employment and all the various forms of subsidies and taxes related to consumption. Even as it stands, however, the study provides a comprehensive comparison of three core elements – contributory insurance, social assistance, and personal income taxation (including direct personal social-insurance contributions) – and their component programs. The results in all countries are based upon conditions that existed in 1979. For Canada, Ontario was the jurisdiction chosen for the evaluation; for the United States, the states of New York and Pennsylvania were selected, because they were committed to quite different levels of income support.

The income level of a family depends on the relative prosperity of the country in which it lives; and government programs that affect family income must be examined in that light. Among the eight countries examined, Canada ranked fifth in per capita GNP. On the whole, Canada was neither leading nor lagging in terms of responsiveness to different types of family situations, whether in the granting of transfers or in the taxing of earned or transfer income. It ranked sixth in generosity to the families targeted by social policy and fifth with respect to the more advantaged group of families. No Canadian families were substantially advantaged or disadvantaged in comparison with that status in other countries. In short, Canada presented a "middling" picture.

The comparisons for particular types of family were made in reference to an unmarried worker receiving the average industrial wage (the average industrial composite wage, in the case of Canada). The Canadian families were assumed to be living in Toronto, renting accommodation, and in good health. The families were characterized in such a way as to represent realistic situations within most countries. Even then, however, certain real-life situations are not adequately captured by representative characteristics. In particular, they do not cover short-term turnover unemployment, where a person receives both earnings and unemployment insurance benefits within a year, nor do they take into account the cost of child care incurred by those families where either a sole-support parent or both parents participate in the labour force.

No Canadian family types were alone at the very bottom of the distribution for their groupings in the international rankings (Table 4-9). Three family types did lag, however; all three were disadvantaged families: a low-earning, sole-support mother raising two children; a family with a single irregular worker; and a family with a long-term unemployed worker. The explanation for this relatively weak showing lies

Table 4-9

Family Net Income as a Proportion of the Average Production Worker's Net Income,[1] and Canada's Ranking among Nine Jurisdictions, by Family Type

	Family net income	Ranking[2]
	(Per cent)	
Family types[3]:		
One parent		
1 Mother not in the labour force	52.5	5
2 Mother employed at half the average wage	75.9	6
Two parents, one earner		
3 One earner at the average wage	114.2	5
4 One earner at half the average wage	73.0	8.5
5 One earner at the average wage, who becomes unemployed at the beginning of the year	76.8	4
6 One earner at the average wage, who has exhausted UIC benefits by the beginning of the year	55.8	7.5
Two parents, two earners		
7 One earner at the average wage, the other at half an average wage	165.0	6
8 One earner at the average wage; the second, at half the average wage, becomes unemployed at the beginning of the year	141.9	4.5

[1] Average earnings are based on the 1979 average industrial composite wage of $14,988.78. Net income is calculated by adding transfers and deducting taxes, contributions, and premiums. The net income of the average production worker was calculated to be $11,684.59 for a single worker living in Ontario.

[2] The rankings indicate how a particular family type fared in Canada relative to how a similar family fared in the other eight jurisdictions when each was compared with its own average production worker's net income. Ties were used where the difference between families in different countries was less than 0.3 percentage points.

[3] All family types comprise two children.

SOURCE Calculations by the Economic Council of Canada, and S. B. Kamerman and A. J. Kahn, "Income Transfers, Work and the Economic Well-Being of Families with Children: A Comparative Study," *International Social Security Review* 3 (1982): 345-82.

in the size and form of the different types of transfer payments, which are more generous in some countries than in others.

While many points of interest emerged in the detailed comparisons, only some will be discussed here. First, consider the single-parent family – a family type that is found with increasing frequency. If, as was traditionally the case, the mother remains at home to care for her children, the family income will be the lowest among all the Canadian families considered – well below the Statistics Canada low-income cutoff. Evidently, this family will require subsidized goods and services, including housing when available. In terms of the relative generosity of the tax and transfer system, Canada's treatment of traditional single parents ranks at the median among the countries examined. Thus the combination of higher social assistance benefits and lower child tax credits and family allowances provides this Canadian family with an income that, while not overgenerous, is not unfavourable, in relative terms, with respect to the income available to similar families in other countries.

In Canada, the main support for single parents who do not work or who work part-time is social assistance – a single program to cover many items of necessity (food, shelter, clothing, and special needs), and one in which the benefits are sharply reduced as income from other sources increases. In some countries – particularly those of northwestern Europe – the range of family-oriented programs is broader, and individual programs are generally available to a much wider range of recipients, even though, in many cases, they receive income from other sources (Table 4-10).[19] While the relative differences are not overwhelming in those cases where the sole-support parent remains at home, they become immediately apparent as soon as he/she joins the labour force.

Suppose that a mother with two dependent children works regularly as a sales clerk at half the average industrial wage (Family 2 in Table 4-9). Provided that other qualifying conditions were met, the family would likely still qualify for social assistance, reduced by $0.75 for every dollar of earnings. While earning a regular wage would move this family up among Canadian families, its ranking on an international basis would be reduced. This worsening would be due to the relatively modest amount of the family-related benefits that are not income-tested in Canada and to the steep reduction in social assistance as earnings increase – features that are not nearly as prevalent in those countries with stronger and more explicit policy commitments with respect to families. Indeed, when combined with changes in other taxes and transfers, this reduction (or tax-back) of social assistance sometimes produces a tax-notch anomaly – i.e., the increase in earnings actually results in a decline in net income.[20]

The situation with respect to the welfare-to-work transition in Canada has worried observers for a long time, and it serves to underline the fundamental problem of high effective tax-back rates on the earnings of social assistance recipients up to about $8,000 (in Ontario in 1979), at which point benefits are completely taxed back. As noted earlier, it is this

Table 4-10

Core Income Transfer Programs, Eight Countries[1]

	Family (child) allowance	Housing allowance	Social assistance	Child support (government)	Unemployment insurance	Other unemployment benefits	Child allowance supplement	Food stamps	Refundable tax credits	Maternity benefits
Sweden	X	X	X	X	X	X[3]	-	-	-	X
West Germany	X	X	X	X	X	X[4]	-	-	-	X
United States										
-New York	-	-	X	-	X	-	-	X	X	X
-Pennsylvania	-	-	X	-	X	-	-	X	X	-
France	X	X	X	X	X	-	X	-	-	X
Canada - Ontario	X	-	X	-	X	-	-	-	X	X
Australia[2]	X	-	X	-	-	X[4]	-	-	-	-
United Kingdom	X	X	X	-	X	-	-	-	-	X
Israel	X	-	X	X	X	-	-	-	-	X

[1] Generic names for programs are used, and significant distinctions are ignored here. For example, the British child benefit is not the same as the child allowance in the Federal Republic of Germany; the Swedish advance maintenance grant is quite different from the Israeli alimony payment.

[2] It is debatable how Australia's income-tested unemployment-assistance and social-assistance benefits should be regarded.

[3] Labour market assistance.

[4] Unemployment assistance.

SOURCE Kamerman and Kahn, "Income Transfers," p. 346.

feature of the transition that has prompted some provinces to experiment with new programs aimed at easing the process. Such programs also apply to traditional family types and provide support to the working poor. Take Family 4 in Table 4-9, for example, in which there are two parents and two children, with only one working at half the average industrial wage – as a cleaner or a security guard, perhaps. Such a family has an income well below the acknowledged poverty line in Canada, and it ties for last place in the international comparison. Again, the main reason for this poor showing is that family-support entitlement programs are relatively more generous elsewhere.

One of the major income security measures in all of the countries studied is unemployment compensation. In this context, the Canadian unemployment insurance program ranks well. In the case of a typical single-earner family in which the breadwinner has been out of work since the beginning of the year (Family 5 in Table 4-9), the Canadian family ranks fourth in the international comparison, even though its income is also below the relevant Statistics Canada low-income cutoff.[21] In the case of a two-earner family where the UI benefits of one earner are combined with the average wage of the second, the results are slightly above the international median and only a little below that for the same family with no unemployment. The relatively high ranking for Canadian families in these circumstances reflects the relative generosity of Canada's unemployment insurance system, in terms of both the level and the duration of benefits. The comparison deteriorates considerably for Canada, however, when the unemployed earner exhausts his/her UI entitlement and has to rely entirely on social assistance, as in the case of Family 6. In such circumstances, the family ranks well down the scale among Canadian families and ties for second last place in the international comparison.

Finally, the overall outcome of the international comparisons is considerably influenced by personal income tax levels, which vary considerably from one country to another. Of all the systems included in the international study, Canada's direct personal-income taxation is among the lightest. Thus many Canadian families receive less generous benefits but pay no taxes, while similar families in other countries receive higher benefits and pay higher taxes. Two-income families in Canada also pay lower taxes than those in most other countries, although the variability of the tax burden in Canada is quite substantial. A major factor here is that income taxes in Canada are based on individual incomes rather than combined family incomes. In the case of a two-earner, fully employed family (Family 7), for example, had one earner alone paid tax on the joint income, his/her tax bill would have been about 38 per cent higher, reflecting the progressivity in Canada's tax structure. While the advantage of individual taxation at this level would not have been sufficient to cover the additional costs of child care for a two-earner family, it would have provided a partial offset.

Thus, while selected international comparisons are always suspect, the overall picture of the Canadian tax and transfer system as it relates to working-age families is mixed. Canada's relative strengths lie in its universal systems of unemployment insurance and needs-tested social assistance; its relative weaknesses lie in the amount of family and child-related income support it accords. The net result is that for some disadvantaged families, the benefit structure is not overly generous by international standards. For single mothers who would like to work, the steep reduction in social assistance benefits that is associated with increasing earnings, together with other disincentives, tends to discourage labour market participation even though the income support provided is at below-poverty levels. Other families living on marginal incomes are also at a relative disadvantage because of the low levels of income support available through family allowances and the child tax credit, compared with those offered by European countries, in particular. While the comparisons are based strictly on the data for Ontario, the basic structure is similar throughout Canada. Some provinces do provide additional support for the working poor, and some also supplement family allowances, but neither of these types of measures is considered in this analysis.

If there is to be some restructuring of the social security system in order to improve the delivery mechanisms, contain costs, or remove inefficiencies and disincentives, then the experience of other countries could be of great value in making the appropriate choices. Recently there have been a number of proposals to restructure the child-benefit package.[22] International comparisons could provide some insight into how such changes might be structured should they be deemed desirable. We shall return to this subject later in this report.

Housing Assistance

Both the federal government and the provinces recognize an obligation to assist persons with insufficient income to gain access to adequate and affordable housing, which is viewed as a basic right of all Canadians. Here, we review government programs that provide housing assistance to families and persons in the lowest-income groups. It seems clear that, although subsidies have continued to grow rapidly, the extension of assistance to low-income Canadians through housing supply policies has not maintained the pace set in the early 1970s. The high financial cost of this type of assistance made it vulnerable when government fiscal restraint became a high priority. Also, the provision of housing that meets both the needs of low-income people and general community concerns has not proved easy. Programs initiated by the provinces to aid such persons by means of shelter allowances have helped to take up the slack, but this approach has not yet developed very far in Canada.

There are Canadians still, particularly in rural areas, who live in dwellings that lack the most basic facilities or have an average of more than one person per room. There are also Canadians who have to spend an inordinate proportion of their income to obtain minimum adequate shelter. The number of households who have (or would have) to spend more than some essentially arbitrary proportion of their income in order to obtain standard shelter (relative to household size) is termed "core housing need." Core need is another, albeit imperfect, indicator of the incidence of poverty.[23] Unlike Statistics Canada's low-income cutoff, it takes into account local rent levels in assessing how much income is left for other needs.

The Canada Mortgage and Housing Corporation (CMHC) estimates that 18 per cent of renters (just over half a million households) experienced core housing need in 1980 – i.e., they were unable to rent adequate accommodation in their locality for less than 30 per cent of their income. This problem was particularly prevalent among women living alone and sole-support mothers (Table 4-11). No current measure of the extent of core housing need among owner-occupiers is available, but earlier studies have indicated that its incidence is much higher among renters than among owners. The CMHC research suggests that the housing affordability problem has not diminished over the past few years. If anything, it has probably worsened.

While core housing need can be seen as a problem of low income, it can be addressed through housing policies. By reducing the cost of housing (and/or perhaps improving its quality, if a family cannot allocate sufficient income to get adequate shelter), it is possible to relieve the poverty problem. A cash transfer – called a "shelter allowance" – the size of which would depend both on the rent paid or the homeownership expenses and on family size and income (perhaps with a ceiling on eligible rent and/or income) would be one way to alleviate the problem. Certain components of shelter expenses can be reduced by a subsidy (which, again, may be related to income), as illustrated by property tax credits and residential rehabilitation grants. Another approach would be to change the supply situation by building or buying shelter and allocating it to the target group at subsidized rents.

While governments have introduced a range of tax and other programs affecting the shelter costs of homeowners, we do not yet have a measure of their impact. In the rental sector, on the other hand, until quite recently at least, governments concentrated on supplying dwelling units targeted at low-income households. For renters in the core-need category, assistance has taken the form of subsidized housing.

The stock of subsidized housing (estimated at more than 260,000 units), though small in relation to the total housing inventory, is not inconsequential when compared with the present number of persons in need.[24] Most are public housing units, built either by the province alone or in partnership with the federal government, or rent-supplement units made available by contract with private landlords, where tenants pay rent on a graduated scale related to income. The CMHC and the participating provinces are committed to these geared-to-income subsidies on a continuing basis. In addition, governments have, by means of interest subsidies and/or capital grants, subsidized entire projects where low-income tenants are part of a mix of income groups. We estimate that about 10 per cent of Canadian tenant households, because they occupy social housing, are helped with their housing expenditures. Some occupants of social housing, however, may not qualify under the core-need 30 per cent rule, and others still pay in excess of 30 per cent of their income on shelter despite the subsidies. Nonetheless, without social housing, the number of tenants paying more than 30 per cent of their income on shelter would increase by approximately one-third.

These statistics refer to the stock of social housing that has been put in place over many years, and they do not necessarily reflect the thrust of current programs. In fact, the CMHC has reoriented its social housing policy, having introduced new programs in 1978-79 (under Section 56.1 of the National Housing Act – NHA) that largely replaced the older public housing programs and the nonprofit and cooperative programs that were intended to add to the stock of social housing. The latter programs were seen to have serious disadvantages.[25] Public housing, for example, required fixed-proportion subsidy sharing by the provinces, although the latter were not equally capable of participating (Table 4-12). It committed governments to open-ended subsidy payments that

Table 4-11

Distribution of Rental Households and Incidence of Housing Need,[1] by Category, Canada, 1980 and 1982

	Rental households, 1980		Distribution of rental households with core housing need, 1980	Occupants of Section 56.1 housing,[2] 1982		Occupants of CMHC social housing,[3] 1982	
	Distribution	Proportion in need		Distribution	Proportion in need	Distribution	Proportion in need
				(Per cent)			
Age of household head							
24 and under	18.2	20.9	20.7	9.5	26.4	3.8	46.6
25-34	30.7	12.2	20.5	32.1	18.2	18.1	52.6
35-44	13.8	13.6	10.2	15.3	30.8	13.0	65.2
45-54	11.1	16.9	10.3	7.3	29.0	8.2	67.0
55-64	10.2	19.5	10.8	8.8	43.3	10.2	77.8
65 and over	15.9	31.5	27.3	26.8	58.1	46.8	79.4
Total	100.0		100.0	100.0		100.0	
Family type							
Single men	17.4	19.7	18.7	8.7	29.0	8.1	69.6
Single women	23.6	30.6	39.4	26.9	51.6	39.9	82.2
Family, no children	20.3	8.8	9.7	17.9	20.1	11.4	50.4
Family, with children	24.8	8.5	11.6	29.2	14.7	17.1	46.8
Single parent, male	1.1	17.7	1.1	1.3	12.8	0.7	55.8
Single parent, female	9.0	35.2	17.4	13.8	60.7	20.9	82.8
Other	3.7	10.3	2.1	2.2	27.0	1.9	62.3
Total	100.0		100.0	100.0		100.0	
Income quintile							
First	20.0	..	..	21.3	97.1	48.8	99.2
Second	20.0	..	..	25.5	47.9	29.9	66.0
Third	20.0	..	..	24.2	4.1	13.2	10.5
Fourth	20.0	..	..	19.5	-	6.0	-
Fifth	20.0	..	..	9.5	-	2.1	-
Total	100.0			100.0		100.0	

1 Housing need is defined as the situation of households unable to afford adequate, uncrowded housing at normal rents without paying more than 30 per cent of their gross income.

2 Excludes Quebec provincial nonprofit housing projects under Section 56.1 of the National Housing Act.

3 Excludes about 3,000 rent supplement households located in Quebec but includes Quebec provincial projects under Section 56.1.

SOURCE Program Evaluation Division, Canada Mortgage and Housing Corporation.

Table 4-12

Distribution of Rental Households with Core Housing Need and CMHC Social Housing Commitments, Canada, by Region, 1950-82

	Atlantic provinces	Quebec	Ontario	Prairies provinces	British Columbia	Canada
			(Per cent)			
Rental households with core housing need, 1980	6.3	25.6	36.4	18.7	13.0	100.0
CMHC social-housing unit commitments, 1950-82	9.0	20.1	44.5	17.8	8.6	100.0
CMHC dwelling unit commitments under Section 56.1, 1978-82	5.2	34.0	32.4	14.3	14.1	100.0

SOURCE Program Evaluation Division, Canada Mortgage and Housing Corporation.

grew rapidly. Moreover, public housing had acquired an unfavourable "social ghetto" image. The federal subsidies available for new projects under the nonprofit and cooperative programs, on the other hand, were no longer sufficient to reduce break-even rents to levels that were affordable to the lower-income groups. The programs relied on the CMHC for capital funding (100 per cent for nonprofit and cooperative projects, and either 75 or 90 per cent for public housing) at a time when the federal government wanted to cut back its financial commitments.

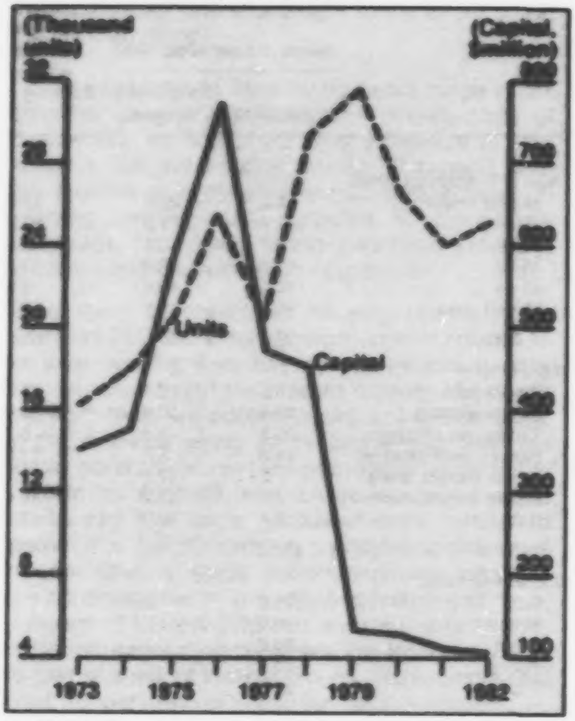
The program changes, therefore, were intended to reduce the federal government's capital commitments, to encourage expansion of the nonprofit and cooperative sector, and to provide more projects with a mix of occupants – both medium- and low-income households. Charts 4-3 and 4-4 provide an indication of the short-term results with respect to these first two priorities. It is the impact on low-income households, however, that is our primary concern here.

In Section 56.1 projects – whether they be public, private nonprofit, or cooperative, and whether they cater to families, senior citizens, or special-need groups – the federal government commits itself to a subsidy determined essentially by the difference between amortization costs at the prevailing mortgage interest rate and those which would ensue at 2 per cent interest over a 35-year amortization period. This subsidy is used, first to reduce rents for all occupants from the level required to cover project costs to the lower end of market rents, and then to subsidize further the rents of those tenants who demonstrate that they have low incomes. Provinces can add to the subsidies in various ways; indeed, their participation is essential if the lowest-income groups are to benefit very much from the program.

For the years 1980 and 1981, when Section 56.1 programs were operating at full potential, commitments were made for almost 40,000 dwelling units and for close to 8,000 hostel beds. These (together with some activity under other continuing programs) boosted the CMHC's total social-housing commitments above the annual average level registered since 1973. In fact, Section 56.1 units accounted for about one-sixth of the total additions to the stock of rental housing through new construction.

Chart 4-3

CMHC Commitments for Social Housing: Number of Units[1] and Capital for Loans and Investment, 1973-82



1 Estimates.

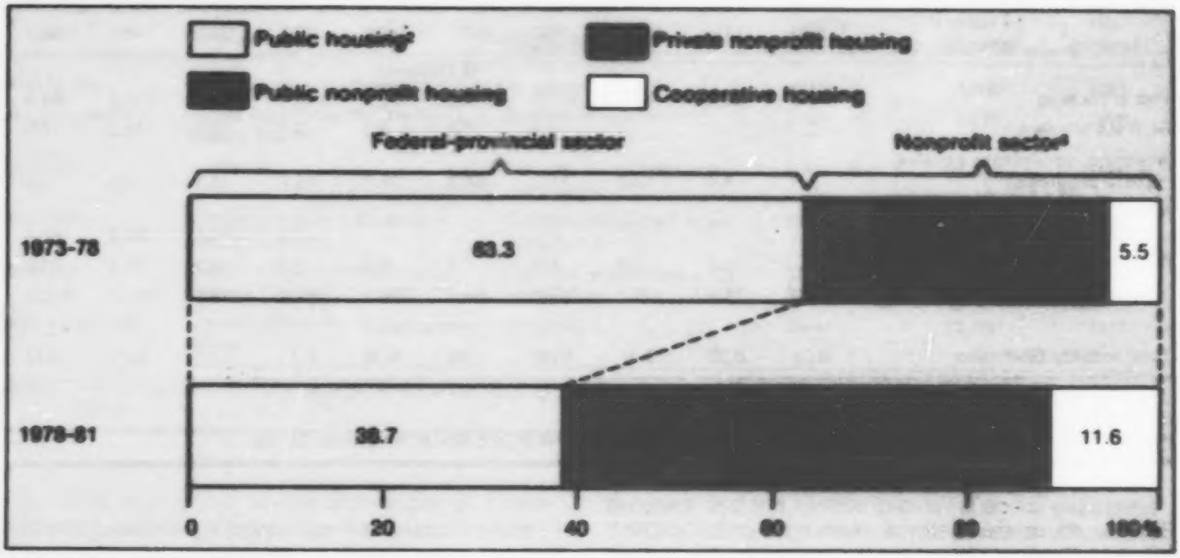
Source Based on data from CMHC.

Although at the time of the CMHC survey of occupants of social housing in 1982, Section 56.1 units constituted a small part of the inventory because few of them were yet in place, useful information was collected for evaluating the new programs as a tool for helping the lowest-income groups. For example, in contrast to public housing, where all tenants are needs-tested and pay rents geared to income, under Section 56.1 only those households who request assistance to reduce rent to below-market levels have to report income. The number of low-income households who are helped and the extent of assistance that they receive vary from project to project. In fact, some 42 per cent of the occupants of Section 56.1 units received an extra subsidy based on their income. About 63 per cent of occupants who were sole-support mothers, and 44 per cent of unattached female households, paid below-market rents. In family housing projects, the average rent of assisted households was about 90 per cent that of unassisted households, whereas in senior citizen projects that proportion was about 75 per cent.

Compared with the total stock of social housing, Section 56.1 has less of the appearance of a residual social program. It caters to more young persons,

Chart 4-4

Distribution of CMHC Commitments for Social Housing, by Type of Program, 1973-78 and 1978-81[1]



1 Excludes rural and native housing projects.
2 Includes rent supplement units.
3 Includes hostel beds. Note that Section 56.1 programs replaced previous nonprofit programs in 1978.
SOURCE Based on data from CMHC.

more husband-and-wife families (see Table 4-11) and, for that matter, more wage earners and more household heads with postsecondary education. But, in the process, "need (or low-income) targeting" has been reduced. The CMHC researchers evaluating Section 56.1 programs concluded that the latter were progressive in their impact on the distribution of income: the lowest-income participants benefited more than did the highest-income participants. At the same time, however, the projects do subsidize rents for many persons who do not have low incomes and do not qualify as having a core housing need. Using Statistics Canada's low-income cutoff, it can be shown that, of the households occupying Section 56.1 units (outside Quebec provincial projects), only 21 per cent could be described as low-income households. According to the CMHC survey, 37 per cent of the Section 56.1 units (outside Quebec provincial projects) were occupied by households with incomes of $20,000 or more in 1981, and 13 per cent were taken by households reporting at least $30,000. Moreover, the objective of mixing low-income households with other income classes has not been entirely successful.[29]

The shifting policy orientation, while it brought a sharp reduction in the CMHC's capital commitments, did not halt the growth in subsidy expenditures on social housing (Table 4-13). The sum paid out by the CMHC in differential interest contributions under Section 56.1 was $186.2 million in 1982. By the end of that year, about 42,000 units were occupied (including conversions, rehabilitations, and hostel beds), yielding a subsidy/cost ratio of $4,400 per unit. Assuming that about one-third of those units were occupied by households with a core housing need, then the annual payments amounted to more than $13,400 per needy recipient. One might justify the expenditure by noting that high interest rates are temporary, that mixed housing and special-purpose homes are highly desirable, and that the unassisted tenants are, after all, paying market rents (albeit at the lower end of the range). Nevertheless, the size of the expenditure appears to be very large.

While most provincial governments have not found Section 56.1 to be a very attractive vehicle for assisting those with core housing need, Quebec is the exception. Indeed, having relied almost exclusively on

Table 4-13

CMHC Subsidy Expenditures on Social Housing, by Program Area, Canada, 1973-82

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
					($ Millions)					
Public housing	46.2	63.4	87.0	117.2	141.1	178.9	240.1	226.5	273.8	364.0
Rent supplement	...	...	3.1	4.9	7.4	9.2	9.1	14.8	16.2	16.5
Nonprofit, cooperative housing (1973 programs)[1]	...	6.4	13.2	21.0	31.3	31.7	25.7	19.1	13.5	10.3
Nonprofit, cooperative housing (1978 programs)[2]	...	...	...	...	...	...	1.0	16.6	60.9	186.2
Rural and native housing program	...	5.7	5.9	6.6	4.3	6.2	7.0	8.3	19.3	23.2
Total subsidy expenditure	46.2	75.5	109.2	149.7	184.1	226.0	282.9	285.3	383.7	600.2
					(Per cent)					
Total subsidy/GNP ratio	0.04	0.05	0.07	0.08	0.09	0.10	0.11	0.10	0.11	0.17

1 Programs under Sections 15.1 and 34.18 of the National Housing Act.
2 Programs under Section 56.1 of the National Housing Act.
SOURCE Program Evaluation Division, Canada Mortgage and Housing Corporation; and data from Statistics Canada.

Section 43 of the National Housing Act for public housing, Quebec had to respond when that program was terminated late in 1978. Commitments under Section 56.1 include a relatively large number of Quebec provincial nonprofit units, though a large proportion of this has not involved any new construction. The provincial projects provide housing for low-income persons, particularly the elderly; 56 per cent of the tenants in those projects in 1981 had incomes below Statistics Canada's low-income cutoff. As a consequence, Quebec supplemented the CMHC subsidy under Section 56.1 to a much greater extent than did the other provinces.

The provinces and the municipalities have been deeply involved in the planning, financing, delivery, and – most importantly – the continuing operation of most of the social housing just described. They have also, over and above their contributions to CMHC housing schemes, developed their own housing programs to help the lowest-income groups. Alberta, in particular, has developed independent housing-supply programs. Income-related property-tax and rental credits or grants offer relief to some tax filers in most provinces. Alternatively, shelter allowances have been introduced to help low-income households (in addition to those receiving social assistance) who spend a disproportionate share of their income on shelter (Table 4-14). To date, the programs are very limited in scope; only five provinces have established shelter allowance schemes (with one also providing assistance to owner-occupiers), and most are limited to the elderly. However, coverage is being extended to those who are near retirement age in some jurisdictions.

These schemes, as presently constituted, do not eliminate core housing need, even among the participants from the eligible groups, but they do enable recipients to consume more housing or other goods and services.[27] Because many recipients live in older housing where rents usually reflect lower building costs, the charge to government of subsidizing shelter expenses at any desired rent/income ratio is much less than if the recipient were to occupy a new high-cost, high-rent unit. Moreover, because of rent ceilings in shelter allowance schemes, low-income family units are motivated to avoid high-cost accommodation.

Currently, the CMHC, with participation by many interested groups, is evaluating its package of social housing programs. Its own research makes it clear that Section 56.1 programs do not represent a major push towards more assistance for those in the greatest need. At the present rate of commitment for additional projects and the observed occupancy rate by those in core need, these programs will serve annually only a minute portion of the more than half a million households estimated to be in core need in 1980 – a figure that undoubtedly increased subsequently as economic conditions deteriorated. Whatever the merits of the CMHC's present social housing programs on other grounds, they are not an adequate vehicle for assistance to those experiencing genuine housing need.

Table 4-14

Provincial Shelter Allowance Programs, Canada, 1981

	Program	Eligibility	Average yearly payment	Number of recipients	Year initiated
Nova Scotia	Rental Assistance Program	All seniors	$475	4,000	1981
New Brunswick	Rental Assistance for the Elderly (RATE)	Seniors in private market units	$495	1,010	1978
Quebec	Logirente	Seniors, subsidized units not eligible	$362	26,747	1980
Manitoba	Shelter Allowance for Elderly Renter (SAFER)	Seniors, subsidized units not eligible	$75/mo.	3,044	1979
Manitoba	Shelter Allowance for Family Renters (SAFFR)	Families, subsidized units not eligible	$86 or $75/mo.	533	1981
British Columbia	Shelder Aid for Elderly Renter (SAFER)	All seniors	$600	12,500	1977

SOURCE Program Evaluation Division, Canada Mortgage and Housing Corporation; and Manitoba Housing and Renewal Corporation, *Annual Report 1980-81*.

The pros and cons of shelter allowances as a form of housing assistance have been discussed for many years at all levels of government. This approach alone does not provide security of tenure. But while they are not a panacea, shelter allowance programs, in our view and given the present environment of limited government resources, offer important advantages. Given the high cost to government of low-income Section 56.1 units already in place (as well as that of public housing), compared with the payments made under shelter allowance programs, and given the variability of rents from one location to another (because of partial rent controls and varying rates of inflation), shelter allowance schemes offer more flexibility in dealing with inadequate shelter situations and could potentially cover a much larger percentage of persons in need than do the present Section 56.1 programs. We believe that careful consideration should be given to them in the current review of the CMHC's social housing strategy.

Conclusion

In this chapter, we have concentrated on how selected segments of Canada's social security system have been functioning, particularly in response to the recent recession, and how they compare to systems in other countries. Apart from programs to retain people in, or return them to, active jobs, the two major systems of income support for working-age persons who cannot find a job or who are unable to work are the unemployment insurance program and the various provincial social assistance plans. Of necessity, there are substantial differences between the target groups and the basis of entitlements in the two systems. Unemployment insurance is precisely that – a contributory program through which working Canadians build up income entitlements in the event they find themselves without a job. Social assistance, being the residual in the safety net, presupposes established need; for the most part, it accommodates those who are not fully employable. With increasing layoffs, it is natural that ways and means should be sought to use UI benefits more productively and to offset the swelling numbers of employable persons who are drawing social assistance benefits. Equally, in our view there is merit in re-examining the current system for providing low-income Canadians with adequate shelter, since it seems too costly, compared with the results.

One area, in particular, where the overall Canadian system may be failing to provide adequate economic support is that of single parents supporting families or of women whose husbands are disabled. In these and other cases of hardship, women seem to be bearing a disproportionate share of the burden. On the other hand, many women are enjoying more career flexibility than ever before. Over the last two decades, the roles and opportunities of women have changed dramatically, although these improvements have often been matched by more demanding personal responsibilities. We turn to these issues in the next chapter.

5 Women and Work: Opportunity for Choice

Equal opportunity of choice for men and women – where "the whole range of emotional and financial burdens and rewards of participating in society, exclusive of pregnancy and child birth, [are] unrelated to one's sex – was the criterion established in *Opportunity for Choice: A Goal for Women*, published seven years ago.[1] The approach taken in that study, which highlighted certain findings of the 1971 census, and its assessment of the socio-economic situation of women warrant our attention today. A well-balanced presentation of the statistical evidence, the study combined positive, forward-looking standards with realistic evaluation. Recognizing the danger of interpretation based on statistical averages, it documented the complexities of the involvement of women in the labour market, the changes that were occurring, and how the obstacles to more effective choice were varied, complicated, and interrelated. By demonstrating that the range of relevant activities extended far beyond the labour market and that, given our economic system and our preference for individual initiative, there were limits to intervention, it provided a realistic context for discussing the policy issues that affect the women of today.

Our own research, using data from the 1981 census, serves to confirm and reinforce those earlier findings. For example, concern about the seriousness of unbalanced family-care burdens as an obstacle to equality of opportunity persists despite the increase in labour force participation by women. Moreover, we note the continued difference between men and women with respect to hours of paid employment. The limited movement of the aggregate male/female earnings ratio is still evident, as are the wide variations in the ratio among subgroups classified by age and level of education. Similarly, the 1981 census reported the movement of women into traditionally male fields, whether these be in universities or the labour market, against the backdrop of a prevailing pattern of sex specialization in training and in occupations. While women have been taking on new activities, some traditional occupations may be acutely vulnerable to technological change. The social programs described in the preceding chapter must, therefore, also be examined from the perspective of how they interrelate with the social and economic adjustments that women will have to face in tomorrow's world.

Growth in the participation of women in the labour force since the Second World War has been common to a number of industrialized countries, but in Canada the change has been quite remarkable (Table 5-1). Although many women worked during the war, in 1950 only one employed person in five was a woman; today, three in seven members of the workforce are women. Increasingly, most young women, along with young men, look forward to spending their prime years in paid employment. The significance of this new reality became particularly apparent during the 1970s, when the combination of high inflation, high unemployment, and rising divorce rates threatened individual and family incomes. And, while we can document these developments with some statistical "snapshots," their implications, particularly in terms of behavioural, social, and legal relationships, offer challenges and dimensions that go well beyond our findings.

Important gaps in earnings and in the amount of time occupied in paid employment persist between men and women in the workforce. These gaps coexist with substantial differences in the types of occupations in which women and men, respectively, are clustered, although significant changes have occurred in recent years. Moreover, many women are impeded by age or by other responsibilities from taking advantage of labour market opportunities; their economic condition, and that of women in situations or communities where there are few wage opportunities, is likely to be much less enviable than that of women in the labour force who suffer from job clustering or the earnings gap.

Historically, the economic condition of women has been affected by many factors, but those which have had perhaps the most significant bearing on their present or potential incomes include:

- their roles with respect to family and household responsibilities;

Table 5-1

Female Participation Rates in Nine Industrialized Countries, 1960, 1970, and 1981

	1960	1970	1981
		(Per cent)	
Canada[1]	30.1	38.3	51.6
United States	37.7	43.3	52.1
Australia	. .	40.4	45.5
Japan	52.7	49.3	46.7
France	41.6	40.1	43.1
West Germany	41.2	38.4	38.5*
United Kingdom	39.5	42.0	46.6*
Italy	33.8	26.8	29.9**
Sweden	. .	50.0	60.5*

*Preliminary figures.

**Rate in 1980.

[1] The rates for Canada in this table, which are drawn from the Labour Force Survey, differ slightly from those in other tables, which are based on census data.

SOURCE C. Sorrentino, "International Comparisons of Labor Force Participation, 1960-81," *Monthly Labor Review* 106, no. 2 (February 1983).

- sex-stereotyping in the socialization process, including in school and in the workforce, particularly with respect to certain occupations, such as nursing, stenographic work, or garment-trade activities;
- the concentration of women in relatively few areas of skill specialization and professional training, which narrows their search for employment and results in occupational concentrations when they arrive on the labour market;
- their relatively greater life expectancy than that of men; and
- the often limited financial resources of single providers, widows, and women living alone in their later years.

Set against the backdrop of these factors in recent years have been the uncertainties inherent in the slower growth of economic activity and of productivity, and in the high rates of inflation and unemployment, combined (except during the 1982 recession) with the continued tilt of job expansion towards the service sector.

Labour Market Participation

The search for improved economic well-being and income security has prompted a growing number of women, particularly married women, to enter the labour market. With progressively more wives working or seeking work outside the home, their contribution to family income has, in many cases, more than offset whatever erosion had occurred as a result of rising inflation and unemployment. Currently, in a traditional two-parent family where the woman works, she contributes, on average, close to one-third of the family income (Table 5-2). Indeed, according to the National Council of Welfare, if women in two-parent families had not worked, the proportion of those families with incomes below the poverty line in 1979 would have risen from one in fourteen to one in eight.[2]

Table 5-2

Average Contribution of Women in the Labour Market to Family Earnings in Two-Parent Families,[1] by Family Status, Canada, 1971, 1975, and 1979

	1971	1975	1979
		(Per cent)	
Two-parent families			
Without children[2]	34.5	33.8	32.4
With children under 6 only	27.9	28.6	28.2
With children aged 6 to 15 only	23.9	25.0	25.0
With children under 6 and children aged 6 to 15	21.6	21.8	25.3
Weighted average	28.9	28.9	28.7

[1] With the head aged less than 65.

[2] For the purposes of this table, a child is defined as being under 16 years of age.

SOURCE Statistics Canada, Survey of Consumer Finances, special tabulations.

Changes in labour demand have also contributed to the increased labour force participation by women. There has been a reduction, over the years, in the relative importance of jobs that were generally considered to be male preserves – in such areas as mining, lumbering, and heavy industry, for example – coupled with significant increases in employment in administrative, educational, and health care services, as well as in other white-collar occupations where the skills of women are increasingly being recognized. As service sector activities have expanded and as employers have attempted to contain wage costs, a growing number of part-time, seasonal, or short-duration jobs have been created. This situation suits many women who are prepared to combine, at least for a while, fairly low earnings with greater job flexibility in order to meet their immediate family responsibilities.

Social, cultural, and institutional factors have also played a very significant role in the increased participation of women in the labour market, by changing their perception of their own role in society. In particular, the advent of more effective methods of family planning, the higher levels of schooling reached by women, and the transformations in traditional family patterns caused by the higher incidence of divorce and separation have been influential. So, too, has Canada's personal income tax system which, unlike that of some European countries (as indicated in Chapter 4), permits separate filing by each family earner, which results in lower marginal tax rates on earnings than would be the case if the earnings of all family earners were combined for tax purposes.

Compared with the other major OECD nations, almost as many women, proportionately, participate in the labour force in Canada as in the United States; fewer than in Sweden; and more than in the rest of Europe (including the United Kingdom) and Japan. Behind the aggregate figures, however, are differences in the institutional practices and the age profile of female employment (Table 5-3). In North America it is common practice for teenagers to have part-time or summer jobs, and the participation rates of teenage girls are quite high. They are also high in the United Kingdom, where relatively fewer young women go on to postsecondary education. In France, Italy, and Japan, however, teenage female participation rates are low. In almost all countries the peak years of labour force activity are those between 20 and 24. During women's prime years, labour force participation is particularly high in Sweden, encouraged by extensive daycare facilities, creches, and labour legislation that provides extensive paternity, as well as maternity, benefits. In Japan there is a sharp drop in economic activity connected with marriage and the birth and rearing of young children, followed by rising participation rates after age 35. Among women aged 55 and over, relatively fewer women in Canada continue to work actively than in the United States or in most of the other leading OECD countries.

During the 1971-81 period the participation rate of women in Canada rose by 13 percentage points, with the increase occurring in all age groups except the oldest and with those aged 25 to 44 showing the highest increase (Table A-8). The participation rates among women in this latter age group in 1981 were almost half as high again as they were a decade earlier. One notes also that the participation rates of women with at least a high school diploma rose quite rapidly during the 1970s – by between 9 and 14 percentage points, depending on the level of schooling (Table A-9). One of the factors associated with the increase in female participation rates appears to be the absence of preschool children in the household, in many cases because women or couples have decided to either delay having children or not have any. Even among married women with preschool children, according to the 1981 census,

Table 5-3

Female Participation Rates in Nine Industrialized Countries, by Age Group, 1981[1]

	Teenagers[2]	20-24	25-34	35-44	45-54	55-64	65 and over	All age groups
Canada	52.2	73.0	62.7	61.6	54.1	33.7	4.3	51.6
United States	52.9	68.9	65.5	65.5	59.9	41.3	8.1	52.1
Australia	61.5	71.1	52.5	58.2	47.8	21.8	2.8	45.5
Japan	18.5	69.7	47.9	59.5	60.5	43.6	14.9	46.7
France[3]	24.8	68.5	67.7	61.4	55.8	38.3	4.3	43.1
West Germany[4]	41.4	71.1	59.5	55.1	49.6	28.5	3.0	38.5*
United Kingdom[4]	64.5	68.5	56.3	68.3	67.8	39.0	2.9	46.6*
Italy[4]	24.2	51.5	47.1	38.6	31.1	14.4	1.8	29.9
Sweden	56.0	81.6	81.4	84.8	83.3	55.6	2.5	60.5*

*Preliminary figures.

[1] The data for France, West Germany, the United Kingdom, and Italy are not adjusted to U.S. concepts. The figures are based on the civilian noninstitutional population, except in the case of Japan, West Germany, and the United Kingdom, where they include the institutional population.

[2] 14 to 19-year-olds in Italy; 15 to 19-year-olds in Canada, Australia, Japan, and West Germany; and 16 to 19-year-olds in the United States, France, the United Kingdom, and Sweden.

[3] Data for 1979.

[4] Data for 1980.

SOURCE Sorrentino, "International Comparisons."

close to half participated in the labour market, as opposed to a little more than one-quarter in 1971 (Table A-10).

While more women are in paid employment, a larger proportion of them are working at part-time or part-year jobs, and a larger proportion are unemployed, than was the case 20 years ago. In 1961 the female unemployment rate was in the area of 3 per cent; a decade ago it was closer to 7 per cent; and today it is between 11 and 12 per cent. And part-time employment has grown – from less than 20 per cent of the women employed in 1961 to over 25 per cent in 1982. As a result of both trends, there has been, in the last decade alone, an average decline of 15 per cent in the annual number of hours worked by women.

Comparing the recession of 1975 with that of 1982 sheds more light on this work pattern. In 1975 one woman in nine worked part-time because she could not find a full-time job, while the others did so because of personal preference or family obligations, because they were still at school, or for various other reasons. During the 1981-82 recession one-quarter of the women working part-time would have preferred a full-time job had they been able to find one; this still left a significant, though reduced, proportion of women who worked part-time by choice.

Each year about 3 per cent of the female workforce quit work because of pregnancy. Of these, about 70 per cent draw UI benefits, and more and more expect to return to work within a reasonable time. Governments have devoted relatively limited resources to setting up daycare services for women with infants and young children. The number of places in daycare centres and approved kindergartens in 1980 was very low (5 per cent), relative to the 2.2 million preschool children in Canada.[3] This does not necessarily imply a severe inadequacy in the social infrastructure, however, since the vast majority of child care arrangements are private. Indeed, a recent study has estimated that over half of all preschoolers are under the care of persons other than their parents during working hours.[4] The study further found that only a small number of working parents (accounting for about one in seven of the children under care) stated that they would like to alter the type of daycare that they were currently using (Table A-11); and, of this group, only a small proportion stated that they would prefer to place their child (or children) in a daycare centre. The survey indicated, too, that less than one in every 25 working women had to leave or to refuse a job during the year in question because of child-care problems. The implications of these findings must be treated with caution, however, because of widespread variations in the availability and cost of alternative types of care; moreover, a rise in birth rates could occur over the next few years and could well produce a daycare problem.

Education and Training

While women have had a slightly higher average level of schooling than men for many years, fewer have entered institutions of higher learning. Twenty years ago women accounted for a little over one-fourth of university undergraduate enrolments and for about one-sixth of graduate enrolments. Moreover, they tended to converge on a few areas of specialization. This has changed dramatically, particularly over the last decade or so. Over the 1972-81 period, the total number of women enrolled full-time in universities rose by 54 per cent, while that of men increased by less than 8 per cent. Today nearly half of the full-time undergraduate enrolment is female; in relative terms, even greater advances have been made at the master and doctorate levels (Chart 5-1). In addition, the areas of specialization chosen by women are now more diverse (Table A-12), and those who continue beyond the undergraduate level are those who have opted in many cases, for new areas of specialization.

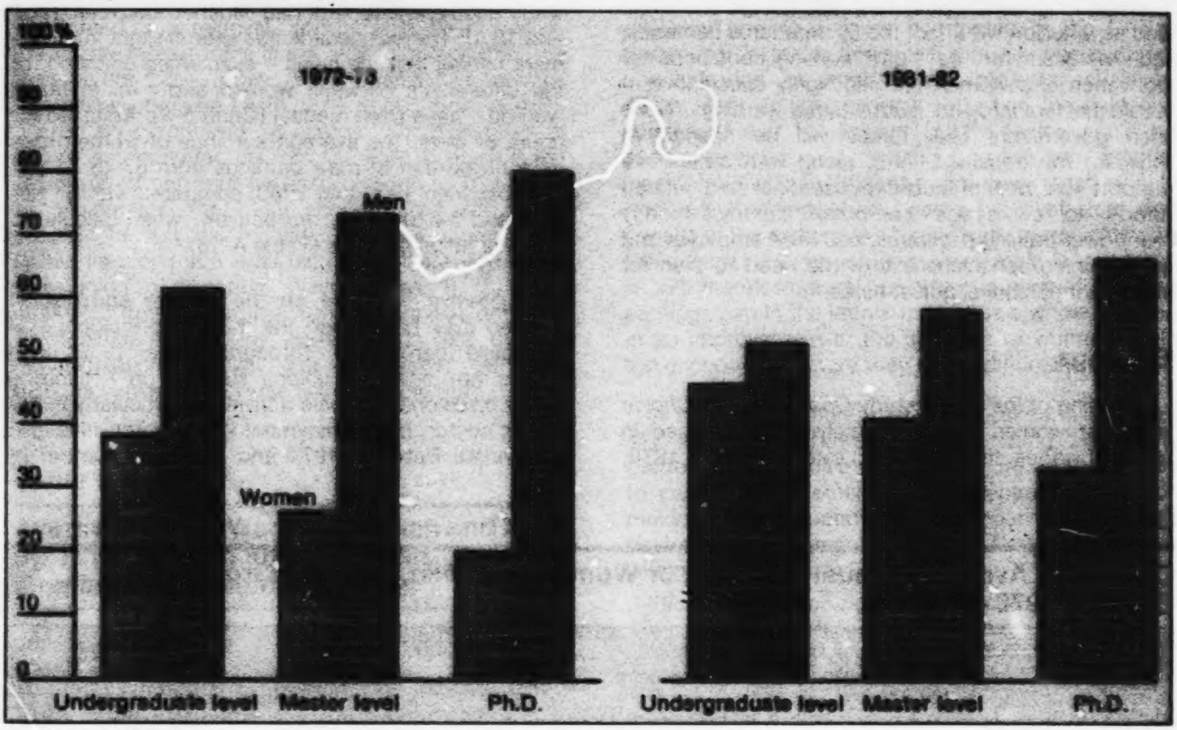
Similar trends are found at the community college level, where over the past 10 years full-time female enrolment increased by 80 per cent, compared with a 50 per cent rise in full-time male enrolement.[5] In 1981 women accounted for about half the enrolment in such programs as general management and administration, data processing, and financial management, although their numbers were still relatively lower in the engineering technologies.

These advances made by women are not unrelated to the efforts that provincial departments of education and other organizations (including women's groups) have made over the past few years to encourage young women to pursue their studies to higher levels and to widen the spectrum of their occupational choices. Clearly, although women continue to represent a high percentage of enrolments in nursing and education sciences, they are also making significant inroads into such fields as agricultural sciences, biology, dentistry, medicine, economics, accounting, business administration, engineering, and law.

The adult training programs available through the Canada Employment Centres encompass both institutional courses and industrial on-the-job and apprenticeship training, designed to enable the trainees to acquire new skills. In the decade to 1982, nearly 438,000 women and 764,000 men took part in the federal government's institutional-training pro-

Chart 5-1

Distribution of Full-Time University Students by Sex, by Level of Study, Canada, 1972-73 and 1981-82



SOURCE Statistics Canada, Post-Secondary Education Section, special tabulations.

gram – a balance roughly in keeping with their distribution in the labour market. The program had special importance for women wishing to re-enter the workforce after spending some years at home. Almost one-quarter of the women trainees had been at home for at least 24 of the 36 months preceding enrolment. Somewhat fewer than one-third of the 350,000 participants receiving on-the-job training in the federal government's industrial-training program since 1976 have been women.

The institutional-training program has not contributed to diversification in the female occupational structure. On the contrary, while many of the young women out of universities and other postsecondary courses have gone into traditionally male occupations, a bare 20 per cent of women among institutional trainees who re-entered the workforce have made a similar choice. Employment and Immigration Canada has recently announced, however, that the apprenticeship of new trades and new specializations will be made more accessible to women. It will also provide for women's associations to apply for grants of up to $50,000 to develop training projects for women with special training needs.

Many women are apprehensive about impending technological changes in offices and industries that may eliminate many activities and render their skills expendable. These concerns have focused principally on the advances of microelectronics and on the informational transformations that are occurring. A recent assessment of the impact of computers and high technology on employment in OECD countries concluded that "overall it is women who form the bulk of information manipulators in Canada, who are expected to bear the brunt of the impact."[6] Another study has noted that the growing supply of female clerical labour confronting a "rapidly collapsing clerical labour demand" in government, banking, financial, and other activities "could, unless appropriate measures are taken, lead to nearly a million women being without employment by 1990."[7]

While judgments about how technological change and its diffusion will affect the occupational demands, job displacements, pay, and working conditions for both men and women are still highly speculative, it would be foolhardy to ignore these warnings. More than government task forces will be needed to facilitate the transition. And, along with others, we support the idea of public educational and related efforts to encourage computer literacy, modify manpower training programs, and raise employer and labour union consciousness of the need to plan for significant personnel adjustments.

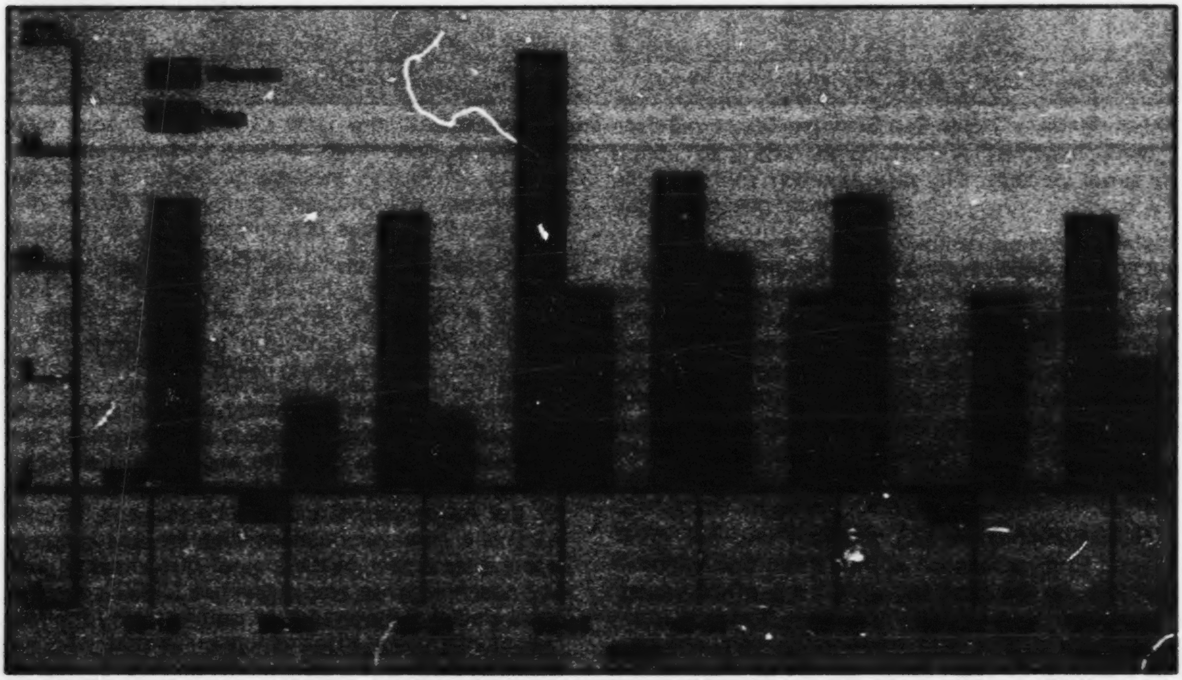
Earnings

A finding of the earlier study *Opportunity for Choice* was that women were extremely disadvantaged in terms of wages, there being no evidence, as of 1970, of a closing of the male/female wage gap that had existed since the Second World War. Indeed, because a greater number of women were working part-time and part-year, the overall earnings gap for wage and salary earners had widened between 1961 and 1970. The last decade has seen a slight improvement overall, but the gains – even when adjusted for the differences between women and men in hours worked – have been modest (Chart 5-2). Adjusted for hours of work, the average earnings of women rose as a proportion of male earnings from 67 to 72 per cent between 1970 and 1980, compared with 51 per cent and 54 per cent, respectively, when calculated on an unadjusted basis (Table A-13).[8]

A positive influence on the relative earnings of women may have been the increased incidence of collective bargaining. Throughout the 1960s and 1970s not only did unions succeed in organizing many traditionally female activities, particularly in the public sector, but employment in these activities also expanded. Between 1971 and 1981 the number of

Chart 5-2

Change in Average Annual Earnings of Women and Men,[1] by Age Group, Canada, 1970-80



1 Excludes those who reported zero or negative income for the whole year preceding the census – i.e., 1970 or 1980. For ease of comparison, 1970 incomes have been adjusted using the consumer price index for 1980.

Source Statistics Canada, 1971 and 1981 censuses, special tabulations.

women in unions increased by over 75 per cent – from 560,000 to 980,000 paid members. This growth, which far exceeded that for men, is all the more remarkable in that many of the jobs taken by women were part-time occupations in the service sector, which tend to be relatively unorganized. Nevertheless, the female labour force is still less unionized than the male labour force: today, one woman in five belongs to a union, compared with close to one in three men. It must be recognized, of course, that high rates of pay reflect many factors, not the least of which is the value added per hour by each employee. This tends to be greater, the more concentrated and more capital-intensive the industry, and the more highly skilled its workforce – all factors that are correlated with union certification. Nevertheless, it is worth observing that for full-time work in unionized activities the male/female hourly wage gap is less than in nonunionized activities. For permanent part-time work, however, the reverse is true (Table 5-4).

Table 5-4

Average Hourly Wage of Women and Men, by Time Worked and by Union Membership, Canada, 1981

	Unionized		Nonunionized	
	Women	Men	Women	Men
	(Dollars)			
Permanent work				
Full-time	8.69	10.17	7.04	9.57
Part-time	8.80	11.08	6.40	7.08
Temporary work				
Full-time	8.08	9.69	5.72	7.29
Part-time	9.22	9.39	5.65	5.73

SOURCE Statistics Canada, Labour Force Survey, special tabulations.

The growing role of women in the public sector has also contributed to the relative improvement in their earnings, since public services embody a wide variety of occupations that tend to be more secure and often better paid than those found elsewhere. In 1980, for example, almost 36 per cent of federal public servants were women. Over the past few years, more women than men have been recruited; and, though parity is still a long way off, more women than men have been making their way into the federal government's middle and upper management.

Some argue that the massive concentration of women in a restricted number of occupations has been largely responsible for the earnings gap – in other words, that an excessive supply of female labour for a limited number of occupations has contributed to relatively low wages and salaries and sometimes poor working conditions. Often these occupations are in sectors where productivity is relatively low. One study conducted in the United States, for instance, indicated that the occupational concentration of women accounted for close to 40 per cent of the earnings gap. And the evidence suggested that the impact of this factor would be even greater if it were possible to refine occupational classifications to the extent of grouping together only positions that require the same types of skills and consist of the same tasks.[9] Improved diversification of the occupational structure in the female labour force should therefore result not only in a narrowing of the earnings gap in the labour market as a whole but also in an improvement in the situation of women within the occupations where they are traditionally found.

A somewhat different view was taken in *Opportunity for Choice*, however. While noting that many predominantly female occupations are not conducive to career advancement or to independent decision making, it concluded that a moderate decline in occupational segregation would likely result in a widening of the earnings gap, since

> Equalizing the occupational distribution would, to a large extent, transfer women from clerical and teaching occupations, where the earnings differential is small, to primary and blue collar jobs, where the earnings gap is large .... Females may be losing ground in occupations where the earnings gap is small and gaining where the earnings gap is large.[10]

This observation, which was based on a very broad occupational grouping, requires amendment in today's context. For one thing, if the U.S. study is any guide, there is need for a much finer, more detailed definition of occupations and tasks. Moreover, there were large shifts in the occupational choices made by women during the 1970s, which altered considerably the occupational structure of the female labour force and was accompanied by some narrowing of the earnings gap.

During the 1970s the number of women working in occupations where men represented more than half the workforce, rose by 0.8 million (or 85 per cent); as a result, in 1981 one in four workers in those occupations was a woman, compared with one in five in 1971. At the same time, however, the numbers of women in occupations where women typically outnumber men showed an even greater increase (about 1 million). Thus the diversification of occupational composition achieved by some women was partly offset by the choices of others who opted for jobs along traditional lines.

Two facts about these developments are particularly noteworthy. First, over the 1970s, as a general rule, the more traditionally male an occupation, the greater the increase in the percentage of women moving into it – admittedly, often from a very low base. Moreover, it was in these occupations that women increased their annual earnings the most – close to 11 per cent annually (compounded), compared with less than 10 per cent among predominantly female occupations over the period. And since many of the traditionally male occupations paid higher-than-average earnings to start with, the women who have entered them have achieved a relatively favourable wage situation.

Indeed, in the 20 highest-paid occupations, where men substantially outnumbered women, the numbers of women quadrupled. And even though most of these women were still relatively young, there was a substantial reduction in the relative earnings gap within those occupations (Table 5-5). On the other hand, in the 20 lowest-paid occupations, where in most cases women outnumbered men, the number of women rose from 750,000 to close to 1.2 million (Table 5-6). Thus, while there was some reduction in both cases in the relative earnings gap between men and women, the relative advances made by women overall have proved to be modest.

When adjustments are made for the fact that in both 1970 and 1980 women averaged fewer hours of work per year than men, the wage gap between women and men narrows somewhat. In the case of women in the 20 lowest-paid occupations, for instance, the average annual earnings amounted to 57 per cent of male earnings in those occupations in 1970 and to 64 per cent in 1980. But, adjusted for the average hours worked in these occupations, the ratios were 71 and 74 per cent, respectively – only a modest improvement. In the 20 highest-paid occupations, the female/male earnings ratio rose from 43 per cent in 1970 to 53 per cent in 1980 and, when adjusted for hours worked, from 54 to 65 per cent – a more tangible improvement, but of course the initial disparities were greater.

Table 5-5

Numbers[1] and Average Annual Earnings of Women and Men in the Twenty Highest-Paid Occupations,[2] Canada, 1970-71 and 1980-81

	Women				Men			
	Number		Earnings		Number		Earnings	
	1971	1981	1970	1980	1971	1981	1970	1980
			(Dollars)				(Dollars)	
Directors general	1,480	2,535	14,745	28,952	39,445	36,320	26,823	59,131
Physicians and surgeons	2,810	6,505	11,774	30,708	25,345	30,255	27,469	57,273
Dentists	280	700	11,434	33,076	6,040	7,605	22,310	54,312
Judges and magistrates	70	200	10,185	31,144	1,195	1,770	21,785	50,791
Lawyers and notaries	770	4,890	8,874	18,416	15,340	26,530	20,218	38,380
Osteopaths and chiropractors	75	285	7,312	13,193	960	1,600	18,676	34,849
Optometrists	95	330	6,689	18,065	1,410	1,365	17,433	39,328
Sales, advertising and purchasing managers	700	13,475	6,286	14,199	15,000	68,925	16,065	28,227
Veterinarians	70	510	6,685	12,590	1,615	2,180	15,202	31,242
Architects	105	490	5,785	15,949	3,835	5,730	14,787	26,415
Air pilot, navigators and flight engineers	20	240	5,325	15,024	4,120	7,580	14,194	32,721
University teachers	3,850	8,030	8,902	19,707	19,355	24,780	14,390	33,274
Members of legislative bodies	100	510	5,371	9,910	1,010	1,795	14,074	30,168
Administrators – teaching	5,680	7,970	9,775	23,097	22,750	25,965	13,998	34,898
Personnel and industrial management	420	6,905	6,219	18,021	3,585	17,920	13,877	29,249
Management occupations	11,630	59,930	5,449	16,074	37,155	189,860	15,237	28,633
Administrators in medicine and health	2,305	5,580	8,622	22,020	2,520	5,245	16,281	34,084
Government administrators	1,510	6,485	7,254	18,870	13,795	22,865	12,971	29,680
Air transport foremen	30	135	8,219	19,179	1,250	1,785	11,378	29,668
Physicists	40	70	7,210	19,872	725	1,165	11,435	28,185
Total	32,050	125,755	8,118	18,253	216,470	481,220	19,024	34,520

1 Excludes those who reported zero or negative earnings for the year preceding the census – i.e., 1970 or 1980.

2 Using Statistics Canada's 1971 occupational classifications, 486 occupations have been combined into 200 groups. Of these 200 groups, the 20 best-paid occupations in 1970 have been chosen on the basis of combined female and male earnings.

SOURCE Statistics Canada, 1971 and 1981 censuses, special tabulations.

Table 5-6

Numbers[1] and Average Annual Earnings of Women and Men in the Twenty Lowest-Paid Occupations,[2] Canada, 1970-71 and 1980-81

	Women				Men			
	Number		Earnings		Number		Earnings	
	1971	1981	1970	1980	1971	1981	1970	1980
Babysitters	17,490	37,505	661	2,640	645	1,315	920	4,311
Waiters(esses), hosts(esses) and stewards	105,885	205,810	1,766	4,418	22,530	35,690	3,182	6,677
Guides, hosts(esses), stewards and others	55,810	39,860	1,908	5,532	8,115	7,455	3,377	8,346
Other farm, horticulture, and animal husbandry	22,800	44,370	1,750	4,696	104,420	125,140	2,632	7,399
Inspecting and sampling, fabrication of textile products	2,035	4,610	2,690	7,320	385	900	5,014	12,311
Sewing machine operators	54,040	85,905	2,861	7,374	6,135	4,665	4,824	10,303
Other fabrication of textile products occupations	9,230	13,230	2,720	6,969	3,850	6,695	4,162	9,750
Other apparel and furnishing service occupations	21,850	24,335	2,693	7,065	10,080	9,780	4,492	9,853
Packaging occupations	35,520	45,025	2,913	7,814	27,495	29,185	3,823	9,073
Other occupations – fishing, hunting, trapping	445	1,870	2,121	4,390	23,960	31,325	3,366	10,044
Tailors and dressmakers	14,930	8,580	2,609	6,936	6,045	4,080	5,283	12,787
Chefs and cooks	35,215	73,820	2,566	6,127	37,195	67,080	4,196	8,284
Knitting occupations	1,990	2,160	2,566	6,867	1,565	1,505	4,534	10,735
Other service occupations	73,565	120,955	2,089	5,864	142,710	181,025	4,129	8,824
Other occupations – library file and correspondence clerks	26,700	39,180	3,235	7,420	6,185	6,690	4,422	8,834
Other sales occupations	165,595	286,395	2,060	5,371	177,130	228,870	4,800	11,783
Shoemakers and repairers	5,855	7,670	2,791	7,377	6,025	4,340	4,253	10,383
Barbers and hairdressers	33,235	46,150	2,872	7,332	20,375	14,530	4,766	12,451
Other occupations – health care	57,665	73,640	3,306	8,607	19,525	21,045	4,969	12,332
Labouring occupation – not elsewhere classified	10,190	14,360	2,712	6,842	74,190	64,645	3,936	9,145
Total	750,045	1,175,430	2,319	6,076	698,580	845,960	4,047	9,559

[1] Excludes those who reported zero or negative earnings for the year preceding the census – i.e., 1970 or 1980.

[2] Using Statistics Canada's 1971 occupational classifications, 498 occupations have been combined into 200 groups. Of these 200 groups, the 20 lowest-paid occupations in 1970 have been chosen on the basis of combined female and male earnings.

SOURCE Statistics Canada, 1971 and 1981 censuses, special tabulations.

These findings both support and modify the observations made in *Opportunity for Choice*. Women are successfully diversifying their activities and penetrating those occupations – particularly professional and managerial positions – which have traditionally been predominantly male-dominated and the best-rewarded. But there is still a very substantial clustering of women in the lowest-paid occupations. And within both the highest- and the lowest-paid activities there has been some progress in narrowing the female/male earnings gaps. When adjusted for hours worked per year, the gaps narrow; and it seems likely that they would narrow still further if they were adjusted for education and experience. Nevertheless, the gaps remain very wide. This suggests that the principle of equal pay for equal or equivalent work must continue to be enforced vigorously. Yet, if there is to be further substantial improvement in the relative earnings of women, the issue goes beyond that to more basic questions of training related to market needs, the balancing of family and career aspirations, and greater occupational diversification. Progress is being made, but slowly, and mostly by the young. Among older women who lack the specialized training needed for many of today's better-paid jobs, the route has been more difficult.

In this connection it is worth noting the views on women in the labour market that were put forward in a technical study recently prepared for the federal Task Force on Labour Market Development:

> Unless an approach which seeks to remove structural barriers is adopted, it is likely that the same forces which operate to segregate women into low pay, low-status jobs in the traditional sector will appear in the non-traditional area as well. Thus the movement of

women into non-traditional trades jobs in itself will not guarantee increasing equality in the labour market.

However, the movement of women into non-traditional jobs (in a wide sense) is an important initiative. Training, job creation and employer incentives to help women move into these jobs should focus on high productivity, stable industries.[11]

Special Problems

Single Parents

This brings us to the special problems of single-parent families, which were discussed earlier in the context of the income-transfer and social-support mechanisms. Owing mainly to the very significant increase in the number of separations and divorces, the incidence of single-parent families has greatly expanded. As a result, one out of six families with children is now a single-parent family, predominantly headed by women. With about one in every three marriages in Canada now ending in divorce, nothing indicates that this trend will slow down in the coming years.

In only about one-third of the cases do the divorced or separated mothers in single-parent families receive a child support award from the courts. Moreover, less than half the debtor ex-husbands honour their responsibilities; and many of those who do, pay less than the full amount ordered by the courts. Furthermore, even when legal steps are taken to recover what is owed, judges are often reluctant to grant arrears.[12] The matter of child support falls under provincial jurisdiction, and each province addresses or defines it differently. Some provinces have taken stronger action to compel the payment of support, and the situation there has improved. Not all provinces, however, exercise reciprocity to facilitate collection from out-of-province spouses, and where such agreements do exist, they are not always easy to apply.

Given the problems encountered in collecting support from their children's fathers and the time and financial demands created by their home responsibilities, combined with the disadvantages that women generally face in competing in the labour market, it is not surprising that so many women heading single-parent families resort to welfare at one time or another. In 1978 over one-third of social assistance cases, on average, were sole-support mothers. We estimate that, just prior to the recession, as many as one-third of such families were on social assistance. The economically disadvantaged situation of this group is confirmed by Statistics Canada's low-income calculations, which show that three out of seven woman-headed families are below the poverty line in 1981.

The economic problems of single-parent families are complex and go beyond a simple call for greater generosity on the part of social assistance programs. In part, their treatment presupposes a more efficient system for enforcing private-support responsibility, as well as programs that will help women to combine employment and parental responsibilities in ways that will enable them to become financially self-sufficient. Programs could be initiated at all levels of government, comprising municipal subsidies to daycare services for families in need, provincial initiatives that would stiffen enforcement of parental-support obligations, and revisions of the social assistance systems, so that more effective and equitable combinations of work and support could be developed. Adult training programs should also prove useful. It is worth noting in this respect, the recent announcement of a doubling of child care allowances for eligible women and men who participate in the National Training Program.

Native Women

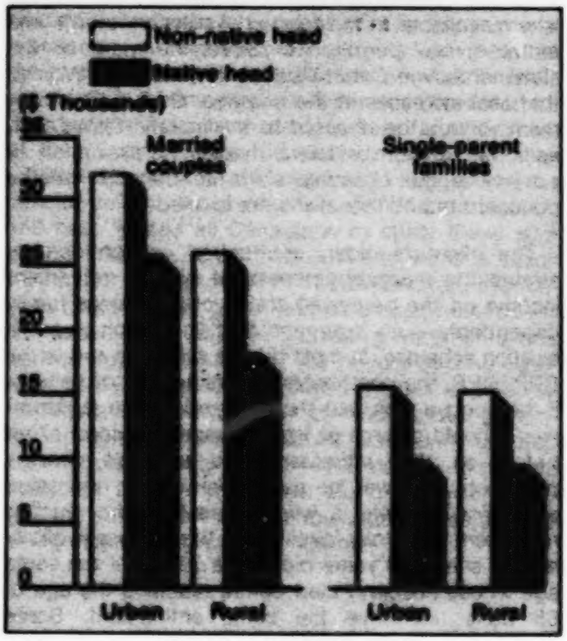
Canada's native population consists of four major groups: status Indians, nonstatus Indians, the Métis, and the Inuit. In spite of the improvement in their living standards over the last 20 years, their average incomes remain well below those of other Canadians as a whole (Chart 5-3). Because native families are generally larger and the proportion of single-parent families among them is almost twice that among non-native families, the actual income gap on a per capita basis is even greater than that shown here. In addition, the average level of education of Canada's natives is substantially lower than the Canadian average; and, often because of their location, their integration into the labour force is limited. Our analysis of the economic difficulties encountered by native women focuses on those who are status Indians – the only group for which detailed statistics are available.

The special problems facing many Indian women living on reserves are numerous[13]:

- Roughly 65 per cent of the Indian population lives on reserves designated as rural or isolated areas,[14] where there are few gainful employment opportunities for women.
- Birth rates among Indian women are substantially higher than the Canadian average.
- The proportion of Indian families with children headed by a sole-support mother is nearly twice as high as the Canadian average, and the size of families is also larger.[15]
- If a status Indian woman marries a non-Indian, a nonstatus Indian, or a Métis, she loses (for herself

Chart 5-3

Average Income of Non-Native and Native Families with Dependants, Rural and Urban, Canada, 1980



Source Based on data from Statistics Canada.

and her descendants) her status and the related benefits, such as the right to live on the reserve, the preferred treatment that bands give female heads of single-parent families, the benefits of the various governmental programs for Indians (such as free tuition and maintenance if she or her children attend university), and her share of the future band fund.[16]

Yet, despite these obstacles, considerable progress is being made, commensurate with a growing sense of identity and assertiveness of the rights of Canada's native peoples. Relative to Indian men and to other Canadian women in general, a greater-than-proportionate number of status Indian women are participating in both the institutional- and industrial-training programs of Employment and Immigration Canada. Also, more are attending university: two decades ago fewer than 150 status Indians (men and women) attended university; today there are nearly 3,000, and among the graduates over 60 per cent are women who, moreover, have chosen a fairly broad range of fields of specialization.

At the primary and secondary school levels, attendance has improved among status Indians, and there are fewer high school dropouts. These results coincide with an increasing willingness on the part of governments to allow and to encourage more initiatives and independence by Indian communities in running their own educational systems. Student enrolments in schools managed by Indian communities are projected to rise from 10,000 in 1981-82 to 20,000 in 1986. This foreshadows a substantial increase in university enrolments.

The shift in the role of governments is evident in other areas. Action to promote and strengthen initiatives by Indian communities, complemented by economic and employment development programs linked to, or made possible by, the resolution of land and related claims on and off the reserves, should broaden the range of economic activities. That, in turn, should promote the hiring of women.

Finally, there is still the federal government's commitment to pursue the complex matter of changing the Indian Act, in consultation with the Indians themselves, in order to eliminate sex discrimination. The amendments will have significant social, cultural, political, and financial repercussions; it is hoped that status Indian women – and perhaps women who have lost their status (depending on the option selected) – will benefit, along with their children, from these amendments.

Women and Pensions

One feature of the aging of Canada's population is the increasing percentage of persons who are of retirement age. According to the census, the proportion of persons aged 65 years and over rose from less than 8 per cent to 10 per cent between 1951 and 1981. Within this group, the proportion of women has been rising steadily and by the year 2000 they are expected to account for 60 per cent of the elderly.[17] Partly because of the longer life expectancy of women, many of these elderly women are without husbands. Indeed, among unattached persons aged 65 and over, women are three times as numerous as men today.

Over the years, many improvements have enabled the elderly to enjoy a better standard of living. But if poverty has been substantially reduced among elderly families, the same cannot be said of the elderly who live alone (Table 5-7). The federal government, in a recent Green Paper, has invited Canadians to put forward proposals on the adequacy and fairness of the retirement income system for discussion and consideration by a Parliamentary Committee. One of the accompanying publications focuses on the pension problems of women, which in turn stem partly from the disadvantages that they encounter in the labour market.[18] As that document indi-

Table 5-7

Income of Economic Families[1] with Head Aged 65 and Over, by Family Status, Canada, 1971 and 1981

	Average transfer income		Total average income	
	1971	1981	1971	1981
	(Dollars)			
Married couples	2,019	7,462	5,894	18,197
Other families	2,018	7,086	8,217	25,473
Unattached persons				
Men	1,310	5,002	3,252	11,021
Women	1,305	4,642	2,492	8,978

[1] The economic family is defined as a group of persons who share the same living accommodations and who are united by blood, marriage or adoption.

SOURCE Statistics Canada, Survey of Consumer Finances, unpublished data.

cates, in comparison with men, women are less frequently covered by employer-sponsored pension plans, owing to their tendency to work part-time or in smaller, nonunionized enterprises where employers are least likely to offer pension plans; they earn less than men, and their pension entitlements are therefore smaller; they are more likely to lose protection because of higher job mobility and poor private-pension portability; they suffer in retirement from the lack of indexing in most private plans and from the deterioration in the real value of benefits over their longer average life-span; and many outside the paid labour force are inadequately protected even by public programs. A major task ahead, therefore, in addressing shortcomings in the social safety nets in the 1980s, will be to improve the mix of public and private pension entitlements for the elderly, particularly for elderly women.

At the moment, many unattached elderly women could be described as being disadvantaged. Because the prevailing pattern for these women during their prime-age years was one of minimal labour force attachment, they have negligible income from contributory pensions; and, by themselves, OAS payments, even when supplemented by GIS benefits, are insufficient to provide adequate support and shelter.[19] Over half the unattached individuals aged 65 to 69, and close to two-thirds of those aged 70 and over, report incomes below the acknowledged low-income levels set by Statistics Canada's 1978 criteria, updated to take account of inflation. The pension system has failed them.

Through time, with more and more women working and building up CPP/QPP as well as private-pension entitlements, this situation will improve. But that is small comfort for those who are now old and alone, and who are attempting to cope with only the OAS/GIS payments and the provincial supplements where available. In the context of pension reform, and as resources permit, we share the view of the National Action Committee on the Status of Women that real increases in the universal OAS/GIS entitlements should be directed to the income-tested GIS, as it is "a more efficient medium if alleviation of poverty is the objective since its benefits can be concentrated on those who are in need."[20]

The plight of older, unattached women demonstrates the inappropriateness of hinging retirement income on the perceived status of women as family dependants – an approach that lingers on in some existing schemes. In most private schemes and in the CPP/QPP, the contributor suffers no loss of benefits if the spouse dies, but the reverse is not true. Moreover, should divorce or legal separation occur, either before or after retirement, the woman's pension prospects may well be put at risk. Other anomalies exist. For example, a wife whose husband reaches retirement age may qualify for the spouse's allowance if she is 60 years old, but a widow of the same age whose husband died before reaching the age of 65 does not have the same entitlement. Some experience real hardship, particularly if their husband's pension had inadequate survivor benefits.

It is important that reform move in the direction of recognizing the contribution made by women to a marriage partnership, whether or not they also have paid employment. For example, it would improve the economic situation of a considerable number of older women if the Canada and Quebec Pension Plans were to extend the principle of joint family assets and sharing of benefits – as presently provided for in divorce cases – by making it universally compulsory and equally applicable in cases of separation, incapacity, or the death of one spouse.

That women be enabled to acquire adequate pensions in their own right is highly desirable; the obstacles that they now face in this regard are well known. Some can be addressed, at least in part, by relatively minor changes in the system. The exclusion, for purposes of pension credit calculation, of those years of absence from paid employment and of the corresponding contributions when women stayed home to care for young children, which is now a feature of the CPP as well as the QPP, is a step in the right direction. Another might be to raise the ceiling on the personal income tax deduction for RSPs and

RRSPs, to encourage the building-up of entitlements in each spouse's name.

As the federal government has observed, however, there is still no consensus among Canadians on the key elements of a solution to the income insecurity of women – on whether there should be an expansion of mandatory earnings-related pension plans (in either the public or the private sector) or on whether there should be a scheme to provide pension protection for persons who have been homemakers for all or most of their working lives. The federal government has advanced a considerable number of suggestions for pension reform, many of which would affect women, and has "invited all Canadians to study these suggested initiatives, and to recommend ways in which they might be improved."[21] The expenditure implications could be very great, and care and prudence will be needed in the dialogue between governments, and between governments and the private sector, especially as it is not evident just how the mix of personal responsibilities, private savings, and various government programs should be joined. But clearly this gap in the social security system – the inability to provide adequate income protection for a significant and growing component of the population – gives a sense of urgency to the proposed reforms.

Conclusion

Over the past two decades more than 3 million women have been added to Canada's labour force. Many, benefiting from more years of schooling and extensive university and postsecondary training, now enjoy well-paid, career-satisfying occupations, some of which were predominantly filled by men in the past. However, the growth in the number of women in the better-paid occupations has been accompanied by an even stronger increase in the number of women in the less-well-paid, often traditionally female, occupations.

Both overall and within specific occupations, there has been a modest reduction in the female/male earnings gap; but progress has been slow, and wide disparities persist. One could argue that the precise implications of an aggregate earnings gap are not readily interpretable and that, in many respects, the gap may not be really indicative of the true situation within any occupation. Nevertheless, the size and persistence of the gap is striking, even within distinct occupational groups, whether measured in relative or absolute terms. While legislation stipulating equal pay for equal work exists in all jurisdictions, the more comprehensive requirement of equal pay for work of equal value still covers relatively few Canadian women.[22] The latter concept, by broadening the basis for comparison, creates the potential for increasing relative (and absolute) pay levels for more women, while remaining within the context of a responsive labour market, the personnel practices of firms, and job description and evaluation systems. Admittedly, vigorous application of this principle will not be easy; indeed, in some circumstances it could even undermine the employment prospects for women if it raised their pay levels above their expected productivity. Nonetheless, it merits serious attention as a lever for eliminating unjustifiable anomalies in pay structures and as a support for women generally, many of whom may be working in enterprises in which their job security and personal bargaining power are very tenuous.

Economic parity with men will obviously not be achieved overnight. Nor, it could be argued, will it necessarily be sought, given the child-bearing concerns of women. The introduction of new technology, if it were accompanied by appropriate adjustments of skills, could be a vehicle for further improvements; or it could erect barriers in the form of dead-end or part-time work, or job dislocations, in traditionally female-dominated occupations.

In short, while some advances have been made to correct the disadvantages encountered by women in the labour market, there persists an underutilization of talent and resources that, while it affects women the most, penalizes all Canadians. A climate of economic recovery offers better prospects for improving the situation of women than does one of stagnation and slow growth, since it opens up a wider array of employment opportunities.

Many women, however, encounter economic problems that can be neither alleviated nor resolved by the labour market alone. If couples have, until now, been postponing parenthood, the proportion of women bearing children could well increase in the 1980s. These parents may need support through daycare and other services. Many other women, for reasons of age, location, health, or family situation, cannot work and are faced with poverty. Widespread problems confront single parents, native and immigrant Canadians, and the elderly. The challenge ahead will be to respond to their needs, in keeping with the requirements of overall fiscal prudence, and to adopt measures that will give support to the autonomy of the individual and encourage personal initiative and responsibility.

6 Conclusions and Recommendations

The Canadian economy is coming out of the deepest recession since the decade preceding the Second World War. Real growth rates this year have been substantial and should average close to 3 per cent overall. But this recovery is building upon almost two years of depressed activity, and output is not expected to reach until well into 1984 the level that was achieved in the second quarter of 1981. There is still a substantial amount of idle capacity in the economy; and, while consumer spending is expected to be relatively buoyant, it is anticipated that net investment will turn positive only next year. Saving rates continue to be high by historical standards, as families and business firms hold back on expenditures in order to improve and realign their debt situation.

Thus while (as indicated in Chapter 3) the prospects for a consumer- and export-led recovery are good, Canadians would be unwise to engage in euphoric anticipation. If our projections are correct, the strength of the recovery over the next few years will be solid but not spectacular. The growth in GNP is expected to remain close to 4 per cent through 1985, but unemployment rates will remain disturbingly high unless a new commitment is made to increase employment.

The international perspective also calls for a recovery in the major OECD countries, with that in the United States having the potential to be among the strongest. One general worry there is the size of the federal debt and the difficulties that the Congress and the Administration are experiencing in reaching a mutually acceptable program to deal with it. While there is no indication that public borrowing to service the debt is now crowding out private investment – which remains weak, as in Canada – it is generally acknowledged that the debt is contributing to uncertainty and to the maintenance by the U.S. Federal Reserve Board of high nominal and real interest rates. High real interest rates in the United States encourage foreign capital inflows, which, in turn, maintain the high exchange rate of the dollar, exacerbate the trade deficit, and encourage protectionist sentiment in the country. They may also discourage new domestic investment and weaken, if not abort, U.S. economic growth in the medium term. Despite this worrisome element, it is our view that, over the coming year, real interest rates in the United States will be somewhat reduced, that inflation rates there will be contained, and that the recovery will be quite strong.

In Canada, the April 1983 budget had a number of twists designed to provide immediate stimulus to the economy, while increasing taxes in 1984 and 1985 – years when the recovery is expected to be well under way and when contracyclical tax initiatives will be offset by increased private spending. Our projections indicate that the federal government's actions, together with the economic recovery, will stay the budget deficit and, over the medium term, lead to its decline relative to GNP. Still, the deficit will remain high in nominal dollars, despite the recovery. One likely reason for this, if our estimates are correct, is that as long as the unemployment rate remains very high, UI benefit expenditures will continue to soar, and there will be pressures to buttress social assistance expenditures under Canada Works and other programs.

The long-term rate of growth of the Canadian economy is largely determined by improvement in its competitive productivity. Current projections suggest that such improvement will be significantly less during the 1980s than in the late 1960s and early 1970s. Experts disagree, however, about the extent to which those earlier gains were real or were inflated by exceptionally favourable terms of trade and by illusory measurements caused by inflation and by the lags affecting price and quantity decisions. But one cannot discount the fact that competitive rigidities and protectionist sentiment and practices have been increasing in the economy in recent years, holding back productivity improvement. Gains in productivity usually presuppose the introduction of new, highly efficient equipment or of different organizational procedures that help to increase output or conserve resources. Generally, they entail managerial initiative and the acceptance and cooperation of labour. Among the lessons learned in recent years is that the extreme adversarial positions adopted in some wage negotiations have been counterproductive. Productivity improvements involve the elimination of some jobs and the creation of others. If the attendant personal dislocations and opportunities are to be addressed in positive ways, there will be a continuing need for informed, mature, and cooperative relationships between labour and management.

Looking to the medium term and taking into account the progress achieved over the past two decades, several issues stand out. The first is demographic. Canada's population is maturing and the number of the aged is growing; at the same time, lower birth rates and lower numbers of young people mean that for several decades yet there will be far more people of working age relative to those in school or retired than there were when the foundations of the nation's systems of social security, postsecondary education, and health care were put into place. Provided that the recovery is maintained and that ways and means can be found to make more productive use of the skills and energies that are now idle, this lighter dependency burden can help to make it easier to meet the financial expenditure needed to provide adequate pensions for the elderly, sound educational facilities for the young, and excellent health care for both young and old. Canadians have come a long way in building a humane and sharing society. We believe that, with prudence and realism, the various strands of social intervention on which generations have come to depend can be improved in their effectiveness without undue prejudice to the real earnings of working Canadians.

Perhaps the most evident changes in recent times have been the rise and persistence of unemployment and the altered role of women, particularly as family providers. It seems likely that these issues will be made even more complex over the medium term, as technological change and the advent of the microchip and robotics displace skills that have become redundant and create skill shortages in many of the new occupations. Thus the resolution of unemployment in this decade will be of foremost importance. Our projections, along with most others that we have seen, show double-digit unemployment rates persisting over the next three to five years. How much of this unemployment will be cyclical and how much will reflect the fundamental structural and technological changes that are occurring in Canadian industry is an issue that will challenge governments at all levels. While it is in the private sector that the vast majority of the new jobs will be found, governments will still have a major role to play in providing much of the skill training and retraining that will be required and in setting policies to encourage business expansion and new investment. Generally, we support job creation programs that are developed with the assistance of, and operated through, the private sector. The recent initiatives undertaken by Employment and Immigration Canada, such as the Canada Works program, coincide with this approach. Clearly, however, unless these efforts are buttressed by private initiatives that provide steady, full-time employment, they alone will be insufficient to bring unemployment rates down to more acceptable levels.

Finally, if the recent past is any guide, it is likely that inflationary pressures will reappear, as the prices of primary products recover and as producers, labour, and management attempt to recover the ground that each has lost in recent years. While the conjuncture of declining aggregate demand and lower world energy prices has led to sharply reduced inflation, greater price flexibility, and more modest wage settlements, these conditions could easily be reversed. Governments at all levels have the responsibility to forestall any new acceleration in prices and costs. In particular, they must contain the price and wage claims of individual groups that are shielded from competition, and they must resist the automatic passing-on of cost increases in those sectors of the economy where prices, output or services are regulated. They must also exercise appropriate surveillance of private sector pricing and collective bargaining settlements, so as to prevent large increases in one area from setting a cost-push pattern for other activities. We shall return to this issue later.

Our Targets

In confronting the years ahead, Canadians could be guided by ideas and attitudes that were moulded during a period marked by high inflationary expectations, mediocre economic performance, and the highest levels of unemployment seen since the 1930s. There is the danger that too many will continue to assume that only sluggish growth is possible, that only tight money and high real interest rates can prevent the return of inflation, that our social security, health, and educational programs must be reduced and offered only to select groups, that Canada needs further protection from the international economy, and that the institutional and federal-provincial rigidities built into the economy have become a fact of life. Many have forgotten the dimensions of Canada's true economic and social potential and are willing to settle for second- or third-rate solutions. The Council rejects this position and believes that, with good common sense, governments, labour, and management can work towards the "high ground."

Twenty years ago, in its First Annual Review (entitled *Economic Goals for Canada to 1970*), this Council laid down the following targets to be pursued by the federal government in developing its monetary and fiscal policies: the achievement of 5.5 per cent annual growth in real output; increased productivity, defined as 2.4 per cent annual growth in real output per employed person; the containment of unemployment rates to 3 per cent; and price increases of no more than 2 per cent annually. In addition, the Council urged that measures be adopted to ensure a relatively stable balance of payments and an equitable distribution of rising incomes among the various regions of Canada. The economy has changed in many ways; the demographic situation is different; and, with growing numbers of workers being occupied in service sector activities, Canada's potential for real economic growth has moderated. Nevertheless, we believe that the current inclination to focus solely on one specific goal for the economy – containing inflation, reducing unemployment, or reducing government deficits, for example – can lead to unbalanced policies and that instead we should, as a Council, go back to the earlier approach of specifying a package of goals for medium-term application. Over the longer haul the package should generally be realistic, and its components should be mutually compatible and nonexclusive. Accordingly, we propose the following targets, to be attained by the Canadian economy over the next four or five years:

1 Restore for Canada as a whole a trend rate of increase in productivity, as measured by real output per employed person, of between 1.5 and 2 per cent per annum.

2 Achieve a trend rate of employment growth of between 2 and 3 per cent per annum, so as to reduce unemployment within, or by the end of, the medium term to between 6 and 8 per cent of the labour force.

3 Keep the trend rate of annual inflation down to 5 per cent or less, recognizing, of course, that there will be variations in inflation rates because of international and domestic factors.

4 Encourage a rate of domestic saving high enough to contain Canada's average dependency on net capital inflows to about 2 per cent of GNP or less.

5 Maintain the objectives and the substance of the existing social policies insofar as they provide benefits to Canadians, but improve the efficiency of their delivery systems and, *where possible*, fill the most urgent gaps in their application.

These targets, which we believe are attainable in the medium term – i.e., in the next three to five years – are not projections, such as were advanced in Chapter 3. Rather, they are normative benchmarks for the future against which governments and public opinion can measure economic performance. Getting from here to there will not be easy, especially since we must start from a base that is operating at 9 to 12 per cent below the economy's potential. The terms of trade for most of Canada's resource-based exports have been depressed, and the overhang of idle capacity and idle men and women is heavy. But, with the spectre of acute inflation receding and with the recovery under way, what more opportune time to commit this nation to the "higher ground."

The first and second targets together, to be consistent, imply a target for overall real economic growth, over the next half-dozen or so years, of between 3.5 and 5 per cent per annum compounded. Indeed, if a substantial reduction in unemployment rates is to be achieved, overall growth rates that are nearer to the top of that range will be required. Considering the lessons of the last two decades, are these targets overambitious? We think not. Given the performance of the other OECD countries, Canada's medium- to long-term potential growth is not that high; and as this country recovers from the depths of the recession over the next few years, the actual average growth rates could well be above the potential rates. Indeed, many times in the past, the growth rates that were recorded from the depths of a recession have exceeded the long-term trend rates.

Considering the unsatisfied collective and individual wants at this time, there is no lack of useful things to do. Canada's public and private capital plant has not kept up with the needs. In the international sphere, Canadians have been constrained in meeting their development and defence commitments. Households have experienced small increases in real incomes; indeed, in many cases real incomes are below their levels of the late 1970s. Purchases have been deferred, and the average age of automobiles and other consumer durables has increased. The gap between the desired and actual stock of housing has increased. Improvements in pension and welfare systems have been put off, and cutbacks in public services have occurred.

As to the attainability of these targets, we believe that our proposed overall growth rates pose no fundamental problem. There is no immediate scarcity of workers or of most kinds of skills, although there could be severe shortages later in the decade if programs of skill development are not modified. For most activities, plant utilization rates are well below potential. There are ample sources of savings here and abroad for domestic investment. There could be some resource or engineering bottlenecks, but world supplies could resolve many of these.

Can the Canadian economy grow at an average rate of 4 to 5 per cent if the growth in world output and trade remains slow? That may be more difficult. But Canadian trade is well diversified, and its share of world trade in most things is such that it could grow without inviting envy or retaliation.

There is, of course, nothing magic about medium-term targets *per se*. It is to be expected that, depending on both internal and external conditions, they will be overshot in some years and undershot in others. Nor would we deny, with the economy so far below its potential, that Canadians will have to exert maximum efforts in order to return to reasonably healthy levels of business activity. Our base case projections – embodying traditional input-output and price relationships – indicate that whereas GNP will average about 4 per cent growth in 1983-85, the subsequent few years will see a cyclical slowing, with little improvement in unemployment. Even the most optimistic CANDIDE scenario, taking 4 per cent average GNP growth out to 1987, will see unemployment remaining at double-digit levels. Whether CANDIDE provides an accurate view of future realities or not, that projected performance is simply not good enough. Indeed, we estimate that getting unemployment down to a range of between 6 and 8 per cent before or by the end of the decade could well call for sustained GNP growth rates of 4.5 to 5 per cent. In terms of targets 1 and 2, this means that both productivity improvements and increases in employment must be sustained at the high end of their target range. *That is the task that confronts us*. And that is our purpose in advocating targets.

We advance no target for government deficits. It will be recalled that our projections in Chapter 3 call for a reduction in the federal deficit as a percentage of GNP as the recovery progresses. Indeed, when adjusted for the inflation premiums attached to past debt obligations, the deficit is relatively small, and the fiscal stance is quite austere. While the federal position was quite restrictive during the recent recession, there can be little doubt that the countercyclical stabilization process inherent in the decline of revenues and increased unemployment insurance payments eased much of the recession's severity. Although we set no deficit target, it is our view, generally, that in the years ahead the federal government should actively seek to reduce its deficit in both nominal and real terms. Our perception in this regard reflects two concerns: first, the longer-run requirements within the private sector for increased net investment; and, second, the possible links between the government debt and the temptation to monetize the burden through expansive monetary policies and inflation. As indicated earlier, the debt load that a country can carry varies substantially over time. And as a general proposition, apart from the intergenerational issue of who benefits and who pays, the debt load in Canada and in most other industrialized nations is not a major impediment to growth. It does, however, put limits on the government's room for manoeuvre, particularly because of the public's perception of the debt burden.

The targets that we have outlined are a package, and the success of each depends in varying degrees on the success of the others. They presuppose a working consensus by which Canadians, through their institutions, outlook, and policies, can pull together collectively to promote these goals.

Productivity and Employment Growth

As indicated earlier, the targets for growth in productivity (between 1.5 and 2 per cent annually) and in employment (between 2 and 3 per cent per year), as well as the unemployment target (down to between 6 and 8 per cent), taken together, call for the achievement of a real annual growth rate of between 3.5 and 5 per cent in Canada over the medium term. The renewal of strong economic growth is fundamental to increases in real personal income and to the strengthening of the revenue base from which government programs can be initiated. For growth to be sustained, the driving impetus must come mainly from the private sector, initially from consumption and then from investment expenditures, buttressed by expanding trade flows. Sustained growth also calls for continuing improvements in Canada's competitive productivity beyond those achieved on a cyclical basis. Government has a role to play, but there is only limited room for discretionary action. Given the extent of Canada's economic interrelationships with the United States and given the fact that the provincial governments now account for the bulk of public spending, federal monetary and fiscal policies must be applied with care. One thing, however, seems evident. Over the next few years, attempts at continuous "fine tuning" of the economy are more likely to increase uncertainty and deter private sector initiative than policies that aim at pursuing a steady course.

As things stand, in addition to the almost 1.5 million Canadians who are now unemployed, there is a substantial number of discouraged workers who will re-enter the labour market once conditions improve. Hence, if unemployment rates are to come down, within our specified time frame, to the levels of our target – between 6 and 8 per cent – employment growth must exceed the growth of Canada's labour force for quite a few years, and most of the additional jobs must be created in the private sector. This means that the working target for employment growth should be at the higher end of the range.

Some may wonder why we have selected a range of between 6 and 8 per cent as the target for unemployment, knowing that this still entails a very high degree of idle resources and human hardship. We expect that this target level could eventually be reduced, but we believe that, given the current level of inflationary pressures, reaching a level of activity that would compress unemployment much further might only trigger a renewal of the spiraling price and wage increases that Canadians have struggled so hard to contain. Furthermore, the 3 per cent unemployment objective of 20 years ago is probably not attainable today, when the common pattern is for two or more members of a family to participate in the workforce for at least some part of the year, thus causing many families to be less mobile than they might have been in the past.

Others may ask whether there is not a contradiction between increasing productivity and reducing unemployment, since the former implies producing more goods and services with fewer workers. Certainly, in the very short run and in isolated instances where there are no markets for additional output, there is such a contradiction. Also, work-sharing programs offer examples where workers agree, in the face of limited sales and for temporary periods, to limit the number of those who would become unemployed, by jointly accepting to reduce their effort and their income. But over the longer term, apart from evolutionary changes in the standard work week and the holiday period, such initiatives have limited application. Economic growth as a means to increased personal income rests fundamentally on the achievement of increased personal output. Thus, in the medium and longer run, increased productivity is essential to generate the additional income and wealth from which additional demand for new goods, services, and employment will emerge. Renewed prosperity and renewed employment growth depend on the basic *complementarity* of labour and management effort, on the one hand, and consumer and investor spending, on the other, despite sometimes fractious but usually healthy disputes over relative shares. While temporary expedients have their place, on a more enduring basis aggregate economic growth rates within the target range of 3.5 to 5 per cent can only be achieved through a combination of rising productivity and rising employment.

Inflation

Persistent and acute inflation undermines consumer and worker confidence by eroding the purchasing power of persons on relatively fixed incomes and contributing to unwarranted real wage losses for many – particularly those workers in the unprotected sectors. But, just as seriously, it jeopardizes this nation's capacity for growth by escalating the risks and uncertainties of longer-term saving and investment decisions and by imperiling the exercise of fiscal discipline by governments as well as the confidence that Canada commands in international trading and financial markets.

Our inflation target calls for a decline to a 5 per cent annual rate. Although inflation rates are likely to remain modest throughout most of 1984, we are not so tranquil about the prospects beyond that period. At that point, with commodity and energy prices moving up, a central problem could be to prevent much of the additional aggregate demand from being absorbed by cost and price increases, leaving the actual increases in output insufficient to meet employment objectives. The Council therefore supports initiatives by both levels of government to monitor price changes and, through a mixture of measures ranging from drawing public attention to excessive situations to "jaw-boning" and selected direct actions, to encourage restraint on the part of both labour and management. In this connection, it will be important to take account of the legitimate framework of industrial relations and collective bargaining; government initiatives that are intended to bear heavily on costs and prices should be the subject of prior consultation with organized labour and employer associations. In addition, as we have indicated on many occasions in the past, the most effective way to contain arbitrary price increases is to expose markets to increased competition from both foreign and domestic producers. This could mean, as the recovery continues, a further judicious reduction in trade barriers and the introduction and application of competition policy measures that have teeth.

Domestic Saving

This raises a further concern about Canada's increasing international exposure as a borrower and lender in world financial markets. This country has traditionally relied on foreign capital for a significant proportion of its net investment, with the result that more enterprises in the metals, minerals, and manufacturing industries come under foreign ownership in Canada than in almost any other OECD nation. In recent years, however, with the domestic saving rate rising quite dramatically, there have been substantial outflows of Canadian equity capital and foreign lendings by Canadian financial institutions, balanced by some reductions in overall foreign ownership. It is normal that, as the nation matures industrially, the base of its domestic savings should increase, enabling it to become more self-sufficient and rendering domestic decision-making more responsive to market opportunities at home and abroad. Encouraging strong domestic savings that are funneled through private pension, savings, and equity funds also offers a healthy alternative to public funding. On the basis of these considerations, we propose as a target for domestic saving that its rate be sufficient to limit net capital inflows into Canada to about 2 per cent of GNP or less.

On the surface, the short- and medium-term interests of Canadians with respect to savings appear to diverge. One of the principal reasons why the recession of 1981 and 1982 was so severe and why the recovery, though promising, has not gone all that far is that consumers have been holding back on expenditures. Admittedly, the slow growth of overall consumer spending has been caused, in part, by the decline in real disposable income, but equally noteworthy has been the exceptionally high rate of household saving out of disposable income. This has reflected a combination of high interest rates and, in the face of high and widespread unemployment, an unwillingness on the part of people to take on obligations that could have a lasting impact on their future standard of living. In the short run, a reduction in the personal saving rate (and hence an increase in consumer expenditures) would be most helpful for the Canadian economy.

But, as indicated earlier, looking further ahead and taking into account Canada's investment needs, growth prospects, and balance-of-payments objectives, it would seem highly desirable for this country to continue to have high average personal and corporate saving rates and to ensure that savings are allocated as efficiently as possible.

Social Programs

In Chapter 4 we have seen how some of the social programs have eased some of the worst hardships of the recent recession, thus helping to prevent widespread social unrest. By international standards, Canada stands out as a nation of enterprise, initiative, and opportunity, with human abilities, geographic expanses, and resources that are as yet untapped, but it is also one with a record of educational, health, income security, and environmental commitment that compares favourably with that of other industrial countries. While Canadians can take considerable satisfaction from this situation, it does have some shortfalls. There are areas where changes in program administration, emphasis, or modes of funding could provide greater efficiency and benefits, at the same time leading to cost reductions.

In examining possible changes to the social programs as they exist, it is important to take into account all costs and benefits, both private and public. There is also, in our view, a need to recognize the merits of programs that provide for all Canadians equally and without discrimination or favour. It has not always been easy to determine where the responsibilities of the federal and provincial governments begin or end, but the Canadian confederation has been knit together and preserved through joint effort and a sense of sharing and mutual concern. It is important to preserve this cohesive spirit. As in the past, the future prosperity of Canadians will depend, in large measure, on the proper balancing of their economic and social aspirations.

Processes and Policies

As we have indicated, there are distinctions that must be made between those measures which are adopted in the short term to help quicken the recovery process and those which will, in the medium and longer term, enable the Canadian economy to achieve some or all of the objectives that we have outlined.

Fiscal and Monetary Issues

At the moment, Canada enjoys a substantial trade surplus and its interest rate structure is, like that in the United States, high relative to those in other OECD nations. This has resulted in an appreciation of the Canadian dollar vis-à-vis most other OECD currencies, in tandem with the strengthening of the U.S. dollar. There has been, it would appear, a deliberate policy of monetary support designed to maintain the Canadian exchange rate in its present range. Over the longer term, in keeping with the targets that we have outlined, it is our view that the exchange rate should be permitted to fluctuate in response to international trade and financial circumstances. While this could introduce some greater volatility in domestic import prices and temporarily contribute to inflation, we believe that it is more important to maintain the growth momentum that will enable Canada to meet the other targets more easily.

The achievement of solid growth and the containment of inflation go beyond domestic-restraint measures and exchange-rate policy. They presuppose the exercise of a balanced monetary policy that is guided not just by one target but rather by a judicious mixture of concerns over the money supply, the velocity of circulation, and real and nominal interest rates. While much debate has occurred in the past, often fruitlessly, between those who would pursue monetarist objectives and those who would rely on traditional fiscal instruments to influence aggregate demand, the objective must be to achieve a proper balance between the two. If there is a central lesson to be derived from the most recent experience, it is that if restrictive policy on both fronts is sufficiently strong, it can reduce inflation, albeit at the expense of a considerable decline in output and employment. In keeping with our view that the federal deficit should be reduced, we believe that the federal government should maintain its policy of fiscal tightness but that, where practical, the Bank of Canada should be prepared to move cautiously to a position of somewhat greater monetary accommodation. This would mean an increase in money supply or velocity, accompanied by a reduction in nominal and real interest rates. Such a policy of fiscal restraint and modest monetary expansion would be a signal to the private sector of the government's commitment to the achievement of investment and growth primarily through private initiative.

This does not rule out selected increases in real expenditures. We applaud, for instance, the adoption by the federal government of the envelope system of expenditures, which encourages the establishment of spending priorities and more efficient fiscal allocation and accountability. It seems clear that, in the coming years, expenditures or tax incentives that contribute directly to economic growth and reduced unemployment will command a high priority, if for no other reason than the fact that the government has much to gain in the form of increased revenues and lower UI expenditures. Accordingly,

1 **We recommend that the federal and provincial governments exercise prudence in their expenditure programs, using the principles embodied in, for example, the envelope system to establish priorities, and that these priorities be balanced in favour of quickening the pace of economic growth and reducing unemployment.**

How the public funds are to be spent will, of course, depend largely on the decisions made with respect to the levels of services and transfer payments and to their division between the two levels of government. In a confederation, perceptions will inevitably differ as to needs and spending priorities, but too often the confrontations that have occurred between the federal and provincial authorities have proved to be counterproductive and self-defeating. Both must work together in order to reach agreement on common goals and on funding methods. The levels of services to the public made possible by shared-cost programs ought to be consistent with the funds that are available, even though the delivery system varies somewhat between provinces. We believe that, within the bounds of fiscal prudence, the maintenance of high standards of universally available health care, education, and social security programs commands a general consensus – one where the federal and provincial governments should be able to reach agreement. If the target levels of growth that we have outlined are achieved, or nearly achieved, there will be little justification for withdrawing, or reducing the levels and quality of, the services that are now available; and there will even be scope for improving the delivery of some.

There is the danger that the recovery of the economy and its subsequent growth could be aborted by a monetary policy that, by keeping real interest rates too high, would discourage the consumption and domestic investment that are necessary to sustain growth. The position of many banking experts is that monetary policy must be responsive primarily to financial markets, with an eye to the supply and velocity of money as well as to nominal interest rates. By this view, the real interest rate is a statistical construct arrived at *ex post* by comparing the nominal interest rate with the measured rate of inflation. As such, it cannot be included as a reliable *ex ante* consideration in the determination of overall monetary policy. While we acknowledge the validity of this view, it is the real rate, rather than the nominal rate, that is the primary consideration for savers and investors. Moreover, most major price changes can be anticipated. Thus, as the economic recovery takes hold,

2 **We recommend that, in keeping with the adoption of a relatively tight and prudent fiscal policy, the Bank of Canada be prepared to adopt a monetary policy designed to keep real interest rates down to the levels consistent with our targets.**

We are aware, of course, that it is difficult, if not impossible, to divorce Canadian monetary strategy from that of the U.S. Federal Reserve Board without incurring substantial swings in investment flows and in the Canadian dollar's foreign-exchange value. To the extent that Canadians can, in the longer run, achieve saving rates on a par with those suggested in our target, there may be less concern about the additional need for foreign investment. And while an eventual deterioration of the exchange rate could impart some upward inflationary pressure in Canada, it could also provide some export and employment stimulus.

Incomes Policies and Inflation

With respect to inflation, it seems clear that the recent recession, in combination with lower world oil prices and the tangible sacrifices made by a great many Canadians, has helped to reduce inflationary expectations and to alter the relationships between competitive forces, variations in the terms of trade, productivity increases, and the average rates of increase in money wages and profits. As in the case of inflation, the process of disinflation inevitably produces some winners and some losers. The goal is to ease the transition, in keeping with the common gains to be achieved through greater price stability.

Along with the severity of the recession, some contend that the government's "6 and 5" program, together with the corresponding wage and price restraint programs implemented by the provinces, has greatly helped to reduce expectations. There are those who would favour institutionalizing these restraint programs at an even tighter level; for now, we are not among them. We believe that all sectors of the economy have a responsibility to keep inflation down and to keep output and employment growth as high as possible. We believe that, in addition to government spending restraint, there must be moderation and restraint in private sector pricing and in the wage negotiations undertaken by labour and management, all carefully and selectively monitored so as to discourage developments that could trigger an inflationary spiral.

The industrial relations system in Canada is founded on the certification of bargaining units and negotiation of collective agreements at the local level. As a result, most settlements reflect the immediate commercial realities that face the bargaining enterprise. In the case of the public sector, or where market power is exercised and labour and other costs are easily translated into price increases or tax hikes, relatively weak bargaining by management may result in settlements that are out of line with productivity increases and the public well-being. In periods of recovery, with sales and revenue prospects burgeoning, managerial bargaining resistance may be especially low. Because comparative bargaining is a natural phenomenon, however, excessively generous settlements in one sector or region, however justified, can set precedents for bargaining parties or arbiters elsewhere, thus leading to a cost-push inflationary spiral of price and wage increases. We believe that, in such circumstances, governments have a responsibility to take action, that they must go beyond "benign neglect," particularly in those areas where they exercise jurisdictional clout. Accordingly,

3 **We recommend that the federal and provincial governments, after consultation with representatives from organized labour and employer organizations, develop ways and means of monitoring price and wage developments in keeping with the policy of restraint, with reasonable discretion to take such action as is deemed necessary to keep inflation at or below the 5 per cent target.**

Many may consider this to be an undue intrusion into the normal supply-and-demand decisions of competitive markets or a half-hearted substitute for the actual regulation of prices and wages. We believe, though, that such measures will be necessary, at least over the next few years, to keep inflationary expectations from getting out of hand. Indeed, what we are proposing here is a lighter and more flexible approach, in preference to the rather heavy-handed type of incomes policy that some have suggested or that was enforced by the Anti-Inflation Board in the mid-1970s. Our proposal would leave wages and prices free to respond to underlying changes in demand and supply and to international conditions, but it would also, at the same time, effectively curb excessive behaviour that could encourage a return to double-digit increases in the cost of living.

Indeed, a review of the recent Canadian experience supports the view that the poor inflation/unemployment tradeoff reflects the development of rigidities and inflexibility in the economy. Although it is difficult to measure these rigidities with any degree of accuracy, they often reflect the nation's inability to reach a working consensus on critical issues. Without, for example, a firm consensus on a predominantly voluntary form of incomes policy of the type that we are suggesting here, too much will likely be asked of fiscal and monetary policy in terms of delivering steady growth and control over inflation.

In this connection, we see new challenges and opportunities in the field of collective bargaining. Some of the experiences observed during the recession, where both parties have pulled together and made sacrifices, may well have nurtured elements of trust that will enable them to work harmoniously in the future. Improved information flows and a greater sense of public purpose in the face of rapid technological change will, it is hoped, help to reduce the adversarial myopia and confrontation that have marked some collective bargaining practices in the past. There have recently been, at the national level, several instances where labour and management worked together in common purpose, and we see a growing recognition of the need for positive relations in collective bargaining and of the responsibilities that labour and management must share jointly in containing inflation, refueling employment growth, and keeping Canada competitive. Otherwise, there could be pressures for stronger, more intrusive, and less flexible measures.

Yet measures to reduce rigidities and inflexibility in the Canadian economy go beyond incomes policies. Production, pricing, and marketing decisions in many sectors have become increasingly insensitive to both domestic and international market forces. Competition policies and regulatory reform have not kept in step with changing market conditions. Geographic barriers have been installed, and the mobility of the workforce appears to have been reduced. Canada, along with other countries, is participating in the trend towards protectionism through nontariff barriers and special contractual and preferential arrangements between countries. Moreover, from a political perspective, there is clear evidence of institutional inflexibility. In federal-provincial affairs, for example, the inability to reach a consensus is an important element of the problems that are threatening the future well-being of Canada's education and health systems.

Eventually, the adjustments necessary for the country and the economy will be made, but the costs and the pain will be less if greater flexibility is achieved. What is required is, by now, almost a trite truism – a greater commitment, developed on a consensual basis, to strengthen the forces of competition in the Canadian economy. Indeed, if Canadians are to achieve the kind of economic targets that we have identified, the real challenge for our country will be to translate this truism into palpable and shared action in a variety of areas. Therefore, to help redress the problems created by rigidities in the economy,

4 **We recommend that governments**

- **continue to attach high priority to regulatory reform and seek methods to render administered prices more sensitive to changing market conditions;**
- **promote competitive conditions in industry and take every opportunity to reduce protectionist practices – in particular, through the introduction and enforcement (by the federal government) of new competition legislation that would effectively remove barriers to entry into various activities and provide adequate safeguards where mergers are likely to reduce competition;**
- **in the field of agriculture, consider new methods to increase the flexibility of pricing and of resource allocation, while maintaining the incomes and financial viability of farmers; and**
- **work together to reduce the burden of regulation in the energy field.**

The foregoing recommendation is, of necessity, rather general. It is not directed at governments alone, although institutionally they are the principal administrators of such policies. Its implementation requires the cooperation of, and some positive initiative by, the many affected groups in the nation, who would have to exchange chimerical short-run interests for the longer-run opportunities that are inherent in more flexible and dynamic markets.

Saving Incentives

We have noted the longer-run need for Canadians to save a greater portion of their incomes for purposes of domestic investment. In the past, institutional investors in Canada have been relatively conservative. Some of the present regulations, which also apply to certain categories of financial institutions (life insurance companies, trust companies, and pension funds), discourage equity investment in small and medium-sized businesses. Others, concerning the types of companies in which funds can be invested, the maximum percentage of their assets that they may invest in any single company, and the maximum percentage of a company's share capital that they may own, are designed to ensure the quality of performance and the integrity of lenders and to protect savers. Indeed, based on the recent experience of some Ontario firms involved in real estate financing, it could be argued that it is time to reinforce the regulations protecting depositors instead of relaxing them. Nonetheless, we believe that there is room for some modest change. Therefore, we repeat the recommendation contained in our report on government credit and credit guarantees[1]:

5 **We recommend that the federal and provincial governments modify their policies to facilitate the strengthening of the equity base of Canadian firms, particularly the small and medium-sized businesses.**

We have been encouraged by recent budgetary measures in this direction, and we urge the retention of the favourable tax treatment now accorded dividend income from Canadian investments. In addition, we believe that, even though inflation has come down, there remain substantial inflation-induced distortions in the application of corporate taxes and that they should be applied more appropriately on real, rather than nominal, corporate profits. We also believe that there are additional incentives that would be worth adopting in the area of personal income taxes. For a number of years, there has been an effective cap put on the amount that taxpayers could deduct for contributions to registered pension plans (RPPs) and registered retirement savings plans (RRSPs). That cap, which is $3,500 for RPP contributions and $5,500 for RRSP contributions at present, has been in place since 1976. Given the past rates of inflation, the real value of this saving incentive has declined by close to 50 per cent. Restoring its original real value would mean increasing the maximum deductions to over $6,500 and $10,000, respectively. This exemption would be concentrated among a fairly small group of taxpayers, however, and according to very crude estimates, it could result in a loss of close to $1 billion in federal tax revenues. More promising, perhaps, as a source of savings may be the broadening of private pension coverage, which will be considered, among other pension reform issues, by a federal Parliamentary committee. Nevertheless, we do see some room for manoeuvre with respect to the present tax deductions for RRPs and RRSPs. Accordingly,

6 **We recommend that, as fiscal conditions permit, the federal government increase the saving incentives inherent in the deduction of contributions to registered pension plans and registered retirement savings plans for personal income tax purposes, by periodically raising their maximum levels.**

Labour Market Issues

We have identified unemployment as a most critical concern for all Canadians over the medium term, and we have expressed the view that it is unlikely that the present set of federal and provincial policies will, alone, be sufficient to bring unemployment below double-digit levels for many years. In our recent report on labour market issues, we recommended a job creation program for the private sector that would contain a tax credit system and, for the longer term, a direct cash wage subsidy.[2] Such a program would not be new; it has already been tried in many forms, both in Canada and elsewhere. The principal target population of the program would be those who bear a disproportionate share of the unemployment burden, particularly the long-term unemployed.

In Chapter 4 we also noted that there has been an increasing tendency to use UI funds for job creation, especially after the onset of the recent recession. The implementation of any new large-scale job promotion programs financed with UI funds would require a new consensus among the federal government, employers, and workers. The original combining of the (then) Department of Manpower and Immigration and the Unemployment Insurance Commission into one overall structure reflected the need to bring together labour market concerns (about job placement, training, retraining, and job creation) and concern for the income needs of the unemployed. Because the UI fund largely represented contributions from employers and employees entitling the unemployed to stipulated benefits, that fund has always been administered separately from the funds expended for traditional manpower purposes. The inclination to use UI funds for job-creation and work-sharing purposes is natural, although it raises a host of legal and other difficulties.

In recent years, most new hirings in the private sector have been by small businesses. One of the difficulties with the job creation schemes that have been developed – and, indeed, with those which this Council has recommended in the past – is that many small businesses are not attracted to them. A tax credit system is not of much benefit when a firm pays little or no taxes; and a direct wage subsidy entails very considerable paperwork and administrative monitoring.

There is always a substantial gap between the gross salary paid by employers and the net salary received by the employee, taking into account the hiring costs and the pension, unemployment insurance, and other contributions paid by the employer. Indeed, it can be claimed that the larger the gap, the more it costs the employer to hire personnel and the less incentive there is for the enterprise to hire or for a person to work. In developing job creation initiatives, the government has some leverage to influence the gap on both sides, by reducing labour costs for the employer and by providing some inducement for people to work rather than collect UI benefits. If the gap is reduced, hiring becomes less costly, and a greater number of jobs will be "created."

When one compares the current outlay in UI benefits (likely to total $11-12 billion this year) to sustain human resources that are idle with the roughly $1 billion in job creation funds administered by Employment and Immigration Canada to render them productive, it is difficult not to wonder whether some more efficient arrangement could be devised whereby a larger proportion of the funds could be directed to employment. UI benefits per unemployed average about $150 per week, and Employment and Immigration Canada's job creation subsidies to employers average about the same amount; yet the two are somehow irreconcilable. What if the two were combined, somewhat along the lines of labour market practices in West Germany, whereby the overall fund and individual entitlements would be used for purposes of employment, training, or unemployment assistance, depending on the opportunities at hand? Earlier job creation experiments and the NEED program in 1982-83 have established that where employers are effectively relieved of a substantial proportion of their wage costs, they will expand employment. Probably much the same would apply to industrial training.

We are attracted, therefore, to the suggestion, put forward by one of our members, that UI benefits be combined with a voucher system that would entitle an employer hiring a person who was drawing UI benefits to recover at least part of the wage costs from the federal government. Under that scheme, each UI beneficiary would be entitled to employment vouchers covering a defined period of time, which could be cashed in by employers. The costs could be met by drawing on monies already available in the UI fund, which in turn could be augmented by funds that are now, or otherwise could be, directed at job creation programs if the voucher system required it. The potential advantages of the scheme are evident: it would reduce the costs of hiring for employers; it would not require the creation of a new bureaucracy because the mechanisms already exist to administer the program; it would be very well adapted to the small and medium-sized businesses that will be the main source of employment growth during the 1980s; and, for the unemployed, it would provide a means to "buy" a job, thereby facilitating their search for work.

We are aware that there are difficulties with this suggestion, just as there are with other job creation proposals. It would obviously favour the hiring of persons who are drawing UI benefits over new entrants into the labour force, and it is not clear how many workers would still be employed once their vouchers ran out. It might thus simply change the faces of the unemployed rather than their numbers. Indeed, a host of questions could be raised about the scheme.

Nevertheless, given the inherent opportunities in the economy, the present situation, which sees close to $1 billion in UI funds being disbursed each month in support of close to 1.5 million unemployed while much less than that is being used to provide jobs or training for perhaps one-fifth of that number of persons, is very distorted. Accordingly,

7 **We recommend that the federal government, along with representatives of organized labour and employer associations, study the possibility of restructuring the unemployment insurance system with a view to integrating it much more effectively with job creation and training programs, and that it consider the feasibility of providing UI beneficiaries with employment vouchers covering all or part of their wage costs to potential employers.**

If the concept of a voucher system has any attraction in the area of job creation, it may have equal appeal in matters of skill retraining. We believe that, as the recovery takes hold, some of the concerns expressed in our report on labour markets will reappear – i.e., the shortage of the new skills that are needed to meet the requirements in many of the new high-technology industries and others that are emerging. As a consequence, renewed emphasis must be given to skill development in the planning and training activities of Employment and Immigration Canada, in cooperation with the provinces. Many persons are already taking skill development courses. The introduction of a voucher system would mean that those who have worked for substantial periods of time and have made considerable UI contributions would be given priority, if they were laid off and their skills became redundant, with respect to extensive retraining for technical occupations and trades. In keeping with these ideas,

8 **We recommend, that, in the course of the review of the current unemployment insurance system just recommended, consideration be given to including some provision whereby workers could build up entitlements that would underwrite the costs of skill retraining and new employment without impinging on their regular or extended UI benefits. While such a system would give retraining priority to older workers who have been displaced permanently from traditional industries, it would have to be supplemented by other programs to meet the needs of younger persons or others with limited or no such entitlements.**

We have not estimated the costs implied by these proposals; obviously, they would hinge on the scale of the initiatives and they would be part of the task of those studying them. What can be said with some surety, however, is that if Canada continues to experience double-digit unemployment rates, the automatic expenditure pressures of the UI system and the accompanying pressures for increased job creation and retraining will remain enormous. To these considerations must be added the losses in production and tax revenues that accompany high unemployment. Some would dismiss ideas of employment vouchers or training entitlements as gimmickry. It must be said, however, that we are not wed to these specific proposals *per se* but rather to a broader rethinking of the purposes not only of Canada's manpower programs – within which the UI system must provide the basic and continuing safety net – but also of UI contributions and entitlements, as well as the responsibilities of the contributors (including the federal government). Inherent, too, are fiscal choices, since the mainstream employment and training programs are funded from general revenue, whereas the larger proportion of UI benefits comes from employer and employee contributions. Overall, without prejudging the outcomes of such considerations, one thing seems evident: when all the sums have been tallied, putting people back to work or usefully upgrading their skills will be less costly than continuing to support idle resources. The most effective way to achieve that is to facilitate the economy's recovery to its inherent robustness. But, along the way, there is room to examine some fundamental employment/training/unemployment alternatives.

Social Issues

In Chapter 4 we examined how some of the other safety nets were working for persons drawing Canada

Assistance Plan benefits or in need of housing assistance. We came to the conclusion that while the CAP was reasonably generous by international standards, very high unemployment and the trend to single-parent families had put extra strain on most provincial social welfare departments. We also noted that there were problems in some provinces with the lack of an adequate transition mechanism enabling persons to move from welfare back to regular or part-time employment because of the very high effective tax-backs that they encountered. Therefore,

9 **We recommend that the federal and provincial governments review their responsibilities under the Canada Assistance Plan with a view to making it easier for social assistance recipients to accept full- or part-time work without being excessively penalized financially and that, where appropriate, they consider the introduction of supplementary transition programs, such as have already been adopted in several provinces.**

We also noted the commitment of all governments to the provision of adequate shelter for Canadians. The federal government, through the CMHC, has offered extensive assistance to low-income families through the provision of public or heavily subsidized housing. This complements the other federal housing assistance that flows to potential homeowners through the tax deductibility of contributions to the Registered Home Ownership Savings Plan and through the specific grants that have been advanced, from time to time, to first-time home buyers. In its present form, however, the CMHC's assistance to low-income rental families is inadequately targeted, in our view, and the benefits are flowing disproportionately to medium-income families. For individuals or families experiencing core-housing need, therefore, the cost per unit is far too high in relation to their needs. Consequently,

10 **We recommend that the federal government, along with the provinces, consider the feasibility of introducing shelter allowances as the principal vehicle for ensuring adequate shelter for those low-income families which are in need of rental housing assistance.**

We recognize, of course, that some shelter allowances are available through provincial and municipal programs and, also, that the present system of NHA-subsidized rental housing cannot simply be abandoned. We see advantages, however, in gradually converting the system to one of shelter allowances that would be more readily directed to families who demonstrate actual need. Whatever administrative difficulties they may entail, it has yet to be shown that such allowances are not a more efficient, and potentially far less costly, instrument for providing adequate housing to individuals and families in need. Moreover, the efficiency demonstrated by the private sector in developing and managing rental projects, including those aimed at low-income families, could be utilized more extensively if this approach were adopted.

We have noted Canada's success in providing health care for its citizens. The health insurance system provides for universal accessibility; it is well established in all provinces; and, by international standards, it provides comprehensive care at reasonable cost.

While Canadian health expenditures as a proportion of GNP remained fairly stable throughout the 1970s, their increase in 1982 has raised concern at both levels of government. With the recession and the slowdown in their own tax revenues, provincial governments have been deeply worried that the block funding for health care provided in the Established Programs Financing arrangements will not be sufficient to cover health care expenditures; the federal government has responsibilities to meet in this regard. As the same time, the federal government and many members of the public are rightly concerned that changes in provincial health care provisions could limit access to services or impose a substantial cost burden on the sick.

We believe that governments must continue to be vigilant in their efforts to contain excessive costs in the health area, particularly since the gradual aging of the population will, by itself, put additional demands on the system. There is, in our view, substantial room for additional preventive care efforts, for the delivery of health care services through alternative modes such as health maintenance centres and community clinics, and for the expansion of paramedic services. There is also substantial room for improving the cost effectiveness of the existing facilities. We endorse the efforts by governments and the health profession to explore and exploit the potential savings that can be derived from these alternative modes of health care delivery and from improved cost effectiveness.

We do not, however, endorse provincial initiatives that would have the effect of transferring to the sick and the aged what are now public expenditure commitments. Pressures to substitute private expenditures on medicare are evident in many provinces. As it stands, three provinces charge monthly family premiums; four impose, or intend to impose, daily hospital charges; and most have allowed physicians to "bill extra," over and above the insurance rates of reimbursement. Extra billing apparently is extensive in Ontario, Alberta, and Nova Scotia

It is important to keep a sense of perspective. As long as patients are free to choose between physicians who opt out of the medicare system and those who do not and as long as accessibility is not affected, the terms of the Canada Health Act are being met. Moreover, although information on extra billing is not publicly available, it is estimated that, even in provinces where it is used extensively, extra billing does not add more than 4 per cent to average provincial medicare costs. The issues of extra billing and hospital user fees, however, are of concern not so much because of their present inequity but because of their potential as activities that could destroy the universal accessibility of Canada's health care system. When extra billing reaches the point where it limits accessibility and enables physicians, particularly in remote areas, to take advantage of the dearth of alternative services in their specialty, that warrants intervention, in our view. Therefore,

11 We recommend that

- **the federal and provincial governments maintain their vigilance in preserving the universality of Canada's medicare program and that they explore ways and means of improving the delivery and quality of services, while containing costs through less expensive efforts such as paramedic and home care services;**
- **the provincial governments collect, and make available, information on the extra-billing practices of physicians;**
- **the provinces curb the application of hospital user fees and, whenever the accessibility of services is hampered, curb extra billing by physicians.**

Education is another area where Canadians can point with pride to the progress that has been made over the past few decades. With the baby-boom generation now aging, there has been a reduction in the numbers of elementary and secondary students, and this has translated into more stable overall real expenditures. Higher enrolments and much greater accommodation of part-time students in the post-secondary sector have maintained expenditure pressures there, but they have also helped to develop highly talented and skilled persons who are able to meet some of the new requirements of today's changing workforce. Nevertheless, there is a problem of inadequate funding in almost every province. In education, as in health care, there are always areas of potential improvement, and quality of education is a clarion cry that inevitably entails more material demands. We note, for instance, that in many provinces, with declining numbers of students overall at the elementary and secondary levels, the teacher/student ratio has risen somewhat, but without much clear evidence of enhanced student performance, at least as measured by university entrance requirements. The reverse may be true of teacher/student ratios in some postsecondary institutions, but there we observe that, foreign students excluded, most Canadian students pay a much smaller proportion of the costs of their educational training than did their predecessors a generation earlier. Perhaps this is as it should be, but it does raise the question whether a combination of higher fee structures and educational bursaries or scholarships might prove more advantageous than the present system. Accordingly,

12 We recommend that provincial governments continue to maintain vigilance with respect to educational expenditures, to ensure that the system is meeting the needs of students adequately and efficiently; we also recommend that they consider various alternative systems of funding for educational institutions at the postsecondary level.

There has been a very substantial entry, over the past two decades, of women into educational courses and professional occupations that were once pre-empted by men. We have noted some of the very positive influences associated with the increased participation of women in the labour force and their increasing role in the economic and political life of the nation. There is, however, still room for improvement in some areas. Our study of the economic role of women leads us to advance the following:

13 We recommend that provincial Departments of Education further examine their curricula and student-counseling processes with a view to encouraging girls and young women, along with young men, to acquire nontraditional skills that will facilitate wider occupational choice in subsequent years and that this be stressed in adult training programs.

A critical element for a parent with young children who wish to work full- or part-time is the adequacy of alternative child care. In many cases, private arrangements are made, to the benefit of all parties, including the children. Municipalities, too, have taken the lead in providing daycare centres that are, for the most part, publicly funded. In some areas, however, there are simply not enough daycare facilities available at a cost that parents on a limited income can afford, and alternative private arrangements may be difficult to make. Accordingly,

14 We recommend that provincial governments review their policies on publicly supported daycare centres to ensure their adequacy in terms of alternative forms of child care.

In Chapter 4 we noted that, while the various strands of family allowance and tax deductions and credits provide substantial child-care help to families, there are special income problems for single mothers and women in low-income families. The basic personal income tax deductions for children offer little or no relief to these families, whereas high-income families benefit greatly by virtue of their high marginal tax rates. We would propose that this situation be reversed, with no loss of tax revenue, so as to tilt the advantage to poorer and single-parent families by eliminating the deduction and augmenting the child tax credit now payable primarily to the mother. In 1982 the value of the child tax deductions to taxpayers was in the order of $1 billion; if they had been redirected, they would have substantially increased the child tax credits for which lower- and middle-income families were eligible.[3] Consequently,

15 We recommend that the federal government consider revising the Income Tax Act so as to convert what are now exemptions for wholly dependent children to income tax credits that would accrue to all claimants with children, up to a given taxable-income level.

In this connection, we support the stand adopted this year by the National Council of Welfare with respect to federal child benefits, and we share the NCW's view that

> Eliminating the children's tax exemption and boosting the child tax credit will reduce the number of children living in poverty and improve the incomes of poor and near-poor families throughout Canada. The rapidly rising number of single mothers, almost half of whom live below the poverty line, will especially benefit from our proposals.[4]

Similarly, there are concerns about elderly women living on inadequate pensions well on into their 80s and 90s and long after their husbands are deceased. Many have lived their lives essentially as homemakers and have had little opportunity to build up any pension entitlements in their own right. The Guaranteed Income Supplement, in conjunction with the basic Old Age Security and the widow's portion of the Canada and Quebec Pension Plans, may suffice, but there is still a substantial number of women who are not eligible for CPP/QPP benefits and have no alternative sources of income. The elderly are, of course, eligible for numerous benefits in cash and in kind, but some further enrichment of the GIS portion of the Old Age Security program, together with the elimination of some anomalies in the CPP/QPP, seems to be warranted.

Moreover, as indicated in Chapter 5, years of raising children at home, dependence on low-wage and periodic or part-time employment, and the rising incidence of marriage breakdown often limit the savings and personal pension entitlements that women can carry into their retirement years. While we welcome the recent changes in the administration of the Canada and Quebec Pension Plans that enable women to drop their nonearning years from CPP/QPP entitlement calculations, we believe that other measures will be required if many women who have followed tradition as mothers and homemakers are to avoid financial uncertainty in their later years. Raising the ceiling of the personal income tax deduction for RSPs and RRSPs, as we have recommended, could help, but the benefits would favour the well-to-do; more to the point are various ideas put forward by women's organizations; some of these ideas have been described in the federal government's recent Green Paper on pension reform. We believe that the federal government should pursue its commitment to pension reform through the Parliamentary committee appointed to study the issue. In that context,

16 We recommend that the federal government, along with Quebec and other provincial governments, as well as interested organizations, give particular attention to ways of improving and expanding opportunities for women to establish pension entitlements in their own right.

International Trade

Finally, there is the matter of Canada's place in world economic affairs. Clearly, as a middle-sized nation, Canada has an expanded role in international trade, even though the slow growth that we and other nations have experienced has encouraged some moves in the direction of protectionism. In the development of industrial policies, various forms of government assistance have been introduced; these have entered into the costs and prices of traded goods, and they are increasingly being scrutinized by producers in other countries who are not equally favoured. We have noted, in particular, the rise in the use of countervailing duties and various forms of retaliatory measures employing both tariffs and quotas. In a recent report we noted that Canada was no less guilty than other countries in its use of nontariff barriers, and we urged the federal government to resist the temptation to create any new nontariff barriers.[5] We still hold to this view. In addition, while we acknowledge that the application of nontariff barriers of various sorts, including domestic preference schemes, will never be completely eliminated, it does seem to us that, in order to avoid counterproductive retaliatory wars, there must be some means of distinguishing between acceptable and unacceptable behaviour. Therefore,

17 We recommend that Canada support the efforts, within the GATT framework and in other international organizations, aimed at establishing a code of behaviour that will enable nations to distinguish between those nontariff barriers which are acceptable under the rules of GATT and those which are unacceptable.

In this connection, we have observed the apparent success of some governments, most notably that of Japan, in developing special relationships with banks and major corporate enterprises with respect to industrial and financial strategies that give special advantage to exporting firms, inhibit imports, and help to shape investment flows at home and abroad. It seems clear that, through such arrangements, exchange rates can, for periods of time, be maintained at levels below their longer-run competitive levels internationally, giving further trade advantage, just as U.S. domestic policy seems to have inflated the U.S. dollar above competitive levels relative to most of its OECD trading partners. These developments hamper trade and promote protectionist sentiment, and we believe that, in GATT and in other international organizations, Canada should press for greater visibility of, and accountability for, such

In *The Bottom Line* we also called for a reduction of tariff and nontariff barriers as the recovery progresses; again, we still hold to this view. In some areas, however, the application of nontariff barriers has stemmed from a desire to protect communities from sudden, harmful plant closures and unemployment. Nevertheless, the use of quotas and the like to maintain these industries is very costly for Canadians, and adequate domestic-adjustment processes are needed as tariff and nontariff barriers are reduced. The federal Labour Employment Adjustment Program (LEAP) is one such mechanism; there are others. We urge that governments re-examine and strengthen these programs in order to facilitate the domestic adjustments that are made necessary by the expansion of trade links.

It seems clear that, with the strong intracorporate trade links that have developed in the North American market and with the lowering of tariff barriers, for some commodities and end products the United States and Canada are, in many respects, close to the status of a free-trade area. This being so, the prospects are enhanced for engaging in bilateral agreements (such as the U.S.-Canada Auto Agreement) that would establish free trade between the two countries in selected sectors of their respective economies. The idea of sectoral free-trade arrangements is one that we considered eight years ago, in a report entitled *Looking Outward*.[6] This idea has been revived just recently in a federal government discussion paper.[7] We have noted the industries proposed in the government's discussion paper as candidates for bilateral negotiations with the United States. Indeed, provided that this move is carefully balanced by domestic adjustment policies, we would suggest that similar possibilities for other sectors be carefully explored. It must be acknowledged, however, that, given the exchange level of the U.S. dollar and with protectionist sentiment in the United States being so high at the present time, the immediate prospects for successful sectoral free-trade negotiations are at best uncertain. Nevertheless, the prospects should brighten as the recovery in world trade works its course.

It is relevant to note here that the production of automobiles and automotive parts in North America is only now recovering from the serious losses caused by the recession and by the automobile industry's failure to remain sufficiently competitive on a worldwide scale. Clearly, though, with the restructuring and modernization that has taken place in recent years, it remains a paramount manufacturing industry and a major source of industrial employment for Canada. The U.S.-Canada Automotive Agreement effectively opened up the North American market to Canadian producers – although they are subsidiaries of giant foreign firms – allowing for economies of scale and specialization that have kept Canadian automobile production competitive with U.S.-produced models. Today, the major U.S. auto makers are merging their knowledge and capital with those of major Japanese and European firms, and their decisions will influence developments on both sides of the border. While Canadian producers have benefited from the upsurge in North American sales of larger vehicles, it is important that Canadian production be sufficiently modernized and diversified to withstand changes in market tastes should world oil prices begin to climb again.

The federal government has before it the report of an industry task force calling for higher domestic content in automobile and automotive parts production. While we welcome the joint initiatives taken by industry and labour, we are mindful that, if they are applied widely by many countries and for many industrial goods, such proposals could seriously jeopardize the trade gains made through GATT – gains that have been carefully nurtured through the years and preserved through the most devastating recession since the Second World War. There is no reason, in our view, to believe that the industry cannot make adjustments in responding to competition. This may require government support or special adjustment programs from time to time. Accordingly,

18 **We recommend that, in considering the future of Canada's automobile and automotive parts industry in the context of the North American trading market and in light of the prospects of economic recovery, the federal government explore ways and means of encouraging production other than through the adoption of explicit trade barriers.**

Canada's involvement in international trade and financial markets has been extensive, and some of our banks have engaged in massive lending through their association with other western banks. At present, the state of some of these loans is quite perilous; and it may be that, unless there is full and complete recovery of industrial activity and trade, some governments will have to provide assistance to avoid nonrepayment. The largest international borrowers – Brazil, Mexico, and Argentina – have recently reached agreement with the International Monetary Fund on a set of economic policies, but their financial situation is still uncertain. Short-term "bridging" credits by national monetary authorities have helped to meet immediate liquidity requirements, but the role of the IMF is crucial. In conjunction with the Bank for International Settlements, which facilitates international lending through the commercial banking system, the IMF and the World Bank have the powers and prestige vested by governments that enable them to examine the legitimacy of economic programs, the financial capacity of countries to carry them, and the ability of those countries to repay. Recently, the IMF has requested the support of its members for a substantial expansion of its General Arrangements to Borrow. Unless these demands to supplement the Fund's present resources are met, its efforts to encourage orderly financing programs could be impaired. Accordingly,

19 **We recommend that Canada contribute its full share to the additional funds requested by the International Monetary Fund and that it be prepared to meet with a similar request by the World Bank.**

Conclusion

Compared with those in our last Annual Review, future prospects appear to be relatively bright this year. We believe that Canadians can look forward to years of renewed growth and prosperity; they can, if governments are prudent and if business and labour are moderate in their expectations, reach out to achieve conditions that correspond, or are close, to the targets that we have outlined in this chapter. The greatest challenge will be to meet the demands of a rapidly changing technology with the skills and efforts of Canadians, in such a way as to increase productivity and lower unemployment. With renewed economic growth, it will be possible to confront, and sometimes remove, some of the inflexibilities and rigidities that have crept into the economy in recent years. We believe that our recommendations are consistent with our targets and with stronger economic growth and personal well-being.

Many of our recommendations entail the consultation and cooperation of both levels of government, of industry, and of labour. If Canada is to achieve the economic performance targets, Canadians must once again be prepared to pull together in common purpose. It is natural that each group will have its own set of priorities and that these will sometimes conflict. But, with the recognition of common objectives and the spirit of enterprise, determination, and cooperation that has marked the best of their heritage until now, Canadians can look forward to new achievements and more favourable growth in the years to come.

In this spirit, we applaud the recent urging of provincial premiers that there be early meetings of federal and provincial first ministers to address the concerns and prospects of the Canadian economy. As we have noted, the provinces today account for substantially more after-transfer spending than the federal government. Thus it is important, for purposes of renewed growth and fiscal stability, that there be some strengthened understanding and harmonization of objectives at both levels. This understanding would recognize that governments at both levels are partners in an economy where interdependence is a fundamental characteristic. It is in the spirit of this understanding that the foregoing targets – which are within the reach of our more optimistic projections – and recommendations are advanced.

Appendix

Table A-1

Health Care Coverage and Costs in Ten OECD Countries, 1960, 1980 and 1981

	Health expenditures as a proportion of GDP		Proportion of population eligible for public health services, 1981		
	1960	1980	Hospital care	Medical care	Pharmaceuticals
			(Per cent)		
Canada	5.5	7.2	100	100	33[*]
United States	5.3	9.6	40	25	. .
Australia	5.1	7.1	100	100	100
France	4.3	8.0	100	99	99
West Germany	4.1	8.0	91[†]	91[†]	91
Italy	3.8	6.5	99[†]	100	100
Japan	. .	6.2	100	100	100
Sweden	4.7	8.3	100	100	100
Switzerland	. .	. .	58[‡]	97	97
United Kingdom	4.0	5.7	100	100	100

[*] 1980.
[†] 1975.
[‡] 1978.
SOURCE Based on data from the OECD.

Table A-2

Real Growth[1] in Seven OECD Countries, 1981-83

	1981				1982				1983
	I	II	III	IV	I	II	III	IV	I
					(Per cent)				
United States (GNP)	1.0	3.3	3.2	0.9	-2.5	-1.6	-1.9	-0.9	1.0
United Kingdom (GDP)	-3.3	-3.3	-3.1	-1.0	—	0.9	2.6	2.6	. .
Japan (GNP)	3.2	4.0	4.9	4.1	3.4	4.2	3.0	3.7	. .
France (GDP)	-1.0	0.5	0.3	1.4	2.1	2.0	1.1	0.5	. .
Germany (GNP)	-2.1	-0.9	-0.1	0.4	-0.8	—	-1.7	-1.9	. .
Italy (GDP)	-1.1	-1.2	1.0	0.3	1.2	0.8	-1.0	-2.5	. .
Canada (GNP)	2.9	5.1	4.0	1.5	-2.6	-5.0	-5.1	-5.0	-1.2

[1] Year-over-year change, seasonally adjusted, by quarter.
SOURCE National Institute of Economic and Social Research, *National Institute Economic Review*, May 1983 and previous issues; Statistics Canada, *National Income and Expenditure Accounts*, first quarter 1983.

Table A-3

Consumer Price Index[1] in Seven OECD Countries, 1981-83

	1981				1982				1983
	I	II	III	IV	I	II	III	IV	I
					(Per cent)				
United States	11.1	9.7	10.8	9.4	7.7	6.8	5.8	4.5	3.4
United Kingdom	12.7	11.7	11.3	11.9	11.1	9.4	8.0	6.2	5.0
Japan	6.6	5.0	4.0	4.2	3.0	2.4	2.6	2.4	2.2
France	12.6	12.8	13.6	14.1	14.0	13.8	10.9	9.5	9.2
West Germany	5.7	5.6	6.1	6.5	5.8	5.4	5.3	4.7	3.7
Italy	20.1	20.6	19.2	18.4	17.0	15.5	16.7	16.7	16.2
Canada	12.2	12.6	12.7	12.3	11.5	11.5	10.6	9.7	7.6

[1] Year-over-year change, by quarter.

SOURCE NIESR, *National Institute Economic Review*, May 1983 and previous issues; *Bank of Canada Review*, May 1983.

Table A-4

Rate of Unemployment[1] in Seven OECD Countries, 1981-83

	1981				1982				1983
	I	II	III	IV	I	II	III	IV	I
					(Per cent)				
United States	7.2	7.3	7.2	8.2	8.6	9.2	9.8	10.5	10.2
United Kingdom	10.3	10.8	12.3	12.1	12.4	12.7	12.7	12.9	13.5
Japan	2.2	2.3	2.2	2.2	2.2	2.4	2.4	2.4	2.7
France	7.0	7.4	7.8	7.7	7.8	7.9	8.1	8.1	8.0
West Germany	3.7	4.2	4.7	5.3	5.6	6.2	6.7	7.1	7.3
Italy	7.6	8.5	8.2	8.9	9.1	9.1	8.6	9.0	9.6
Canada	7.4	7.2	7.4	8.4	8.9	10.5	12.1	12.7	12.5

[1] Seasonally adjusted, by quarter.

SOURCE NIESR, *National Institute Economic Review*, May 1983 and previous issues; *Bank of Canada Review*, May 1983.

Table A-5

General Government Financial Balances, Seven OECD Countries, 1979-82[1]

	1979	1980	1981	1982[2]
	(Per cent of nominal GNP/GDP)			
United States	0.6	-1.3	-1.0	-3.8
United Kingdom	-3.2	-3.3	-2.5	-2.0
Japan	-4.8	-4.5	-4.0	-4.1
France	-0.7	0.3	-1.9	-2.6
West Germany	-2.7	-3.2	-4.0	-3.9
Italy	-9.5	-8.0	-11.7	-12.0
Canada	-1.9	-2.1	-1.2	-5.3

[1] Estimated on the U.N. System of National Accounts (SNA) basis except for the United States, the United Kingdom, and Italy, which are calculated on a national-income-account basis.

[2] Estimates.

SOURCE OECD, *Economic Outlook*, July 1983.

Table A-6

Current Account Balance as a Proportion of GNP in Seven OECD Countries, by Quarter, 1981-82

	1981				1982			
	I	II	III	IV	I	II	III	IV
	(Per cent)							
United States	0.1	0.1	—	—	—	0.1	-0.2	-0.2
United Kingdom	1.1	0.6	0.1	0.6	0.3	0.1	0.3	0.7
Japan	-0.8	0.6	1.4	0.7	-0.4	1.0	1.1	0.8
France	-0.4	0.2	-0.3	-0.4	-0.6	-0.8	-0.8	-0.6
West Germany	-0.6	-0.4	-0.7	0.6	-0.1	0.1	-0.3	0.7
Italy	-1.3	-0.8	-0.1	-0.2	-1.0	-0.3	. .	. .
Canada	-1.1	-1.9	-3.1	-0.8	-0.1	1.1	1.2	0.2

SOURCE OECD, *Main Economic Indicators*, June 1983; International Monetary Fund, *International Financial Statistics*, June 1983; and Statistics Canada, *National Income and Expenditure Accounts*, first quarter 1983.

Table A-7

Gross Annual Commitments of Differential Interest Contributions[1] by CMHC under Section 56.1 of the National Housing Act, by Province or Territory, 1978-82

	Number of loans	Number of dwelling units	Number of hostel beds	CMHC contribution commitments
				($ Thousands)
Newfoundland	65	996	220	7,705
Prince Edward Island[2]	24	94	245	936
Nova Scotia	283	1,483	622	9,346
New Brunswick	82	1,217	1,006	8,049
Quebec[2]	1,156	28,432	2,391	97,118
Ontario	535	24,124	2,455	136,498
Manitoba	107	2,994	709	15,181
Saskatchewan	261	4,200	685	22,687
Alberta	170	3,322	589	24,779
British Columbia[2]	407	10,489	4,622	95,736
Yukon Territory	10	86	–	527
Northwest Territories	5	60	–	851
Canada	3,105	77,497	13,544	419,413

[1] The CMHC subsidies are determined by the difference between amortization costs at the prevailing mortgage interest rate and those which would ensue at 2 per cent interest over a 35-year amortization.

[2] Preliminary.

SOURCE Canada Mortgage and Housing Corporation, *Canadian Housing Statistics* (Ottawa: CMHC, 1982), Table 60.

Table A-8

Participation Rates of Women and Men,[1] by Age Group, Canada, 1971 and 1981

	Women		Men	
	1971	1981	1971	1981
	(Per cent)			
Age group:				
15-19	37.0	51.2	46.6	55.0
20-24	62.8	78.2	86.5	92.0
25-34	44.5	66.2	92.6	95.8
35-44	43.9	64.6	92.8	95.6
45-54	44.4	55.9	90.3	92.7
55-64	34.4	35.4	80.1	77.8
65 and over	8.3	5.3	23.6	17.1
All age groups	39.9	52.9	76.4	79.4
	(Thousands)			
Total participants	3,053	4,938	5,760	7,149

[1] For statistical reasons, the 1981 participation rates exclude persons living in institutions. Had these persons been included, the female participation rate for 1981 would have been lower by 0.7 percentage points, while the male rate would have remained the same.

SOURCE Statistics Canada, 1971 and 1981 censuses, special tabulations.

Table A-9

Participation Rates of Women and Men,[1] by Educational Attainment, Canada, 1971 and 1981

	Women		Men	
	1971	1981	1971	1981
	(Per cent)			
Secondary school or less	34.3	43.5	71.0	71.4
Nonuniversity diploma or certificate, or some university without degree	55.5	67.3	88.0	89.3
Bachelor degree certificate or diploma below bachelor's	63.2	75.9	90.0	91.9
Postgraduate university degree	69.4	80.1	91.1	92.2
All levels[1]	39.9	52.9	76.4	79.4

[1] For statistical reasons, the 1981 participation rates exclude persons living in institutions. Had these persons been included, the female participation rate for 1981 would have been lower by 0.7 percentage points, while the male rate would have remained the same.

SOURCE Statistics Canada, 1971 and 1981 censuses, special tabulations.

Table A-10

Participation Rates[1] of Women and Men, by Family Status, Canada, 1971 and 1981

	Women			Men	
	1971	1981	Numerical increase	1971	1981
	(Per cent)		(Thousands)	(Per cent)	
Married					
Without children[2]	40.6	49.8	656	73.5	72.7
With children under 6 only	27.1	47.7	271	94.0	96.8
With children aged 6 to 15 only	40.3	59.3	314	92.8	95.0
Single and other[3]					
Without children[2]	45.1	53.9	545	62.1	71.3
With children under 6 only	40.1	53.3	32	84.9	89.1
With children aged 6 to 15 only	53.8	66.5	68	85.0	90.4
All participants	39.9	52.8	1,885	76.4	79.4

[1] Since these rates are calculated on the basis of family status, they do not include people living in institutions, commercial establishments, or community centres, such as hotels, motels, hospitals, military camps, prisons, etc.

[2] For the purposes of this table, a child is defined as being under 16 years of age.

[3] Includes separated, divorced, and widowed women and men.

SOURCE Statistics Canada, 1971 and 1981 censuses, special tabulations.

Table A-11

Distribution of Preschool Children Whose Parents Would Prefer to Change Care Arrangements, by Mother's Age, Canada, February 1981

	Number of children in child care	Number of children whose parents would prefer other arrangements	Rate of complaints
	(Thousands)		(Per cent)
Age of mother:			
15-24	167	21	12.4
25-34	793	119	15.0
35 and over	173	25	14.4
Total	1,133	165	14.5

SOURCE "Survey of Child Care," in Statistics Canada, *The Labour Force*, Cat. 71-006, August 1982.

Table A-12

Distribution and Proportion of Full-Time Female University Students, by Specialization, Canada, 1972-73 and 1981-82

	Distribution		Proportion of women in total enrolment	
	1972-73	1981-82	1972-73	1981-82
	(Per cent)			
Agricultural and biological sciences	8.1	6.6	39.5	50.4
Education	43.8	39.3	49.4	57.6
Engineering and sciences	0.7	2.7	2.8	10.5
Health sciences	10.3	8.9	44.6	61.9
Dentistry and medicine	2.0	2.3	19.9	35.1
Nursing	4.6	3.7	98.1	97.3
Humanities	14.0	9.7	49.5	57.4
Mathematics and physics	3.6	4.1	22.6	26.7
Social sciences	19.4	28.7	29.3	44.4
Economics and commerce	2.8	12.0	11.8	35.2
Law	1.5	2.3	17.9	39.8
Total	100.0	100.0	37.2	45.9

SOURCE Statistics Canada, Post-Secondary Education Section, special tabulations.

Table A-13

Average Annual and Hourly Earnings of Women and Men,[1] by Educational Attainment, Canada, 1970 and 1980

	Women				Men			
	Annual earnings		Hourly earnings		Annual earnings		Hourly earnings	
	1970	1980	1970	1980	1970	1980	1970	1980
	(Dollars)							
Secondary school or less	3,087	7,926	2.15	6.57	6,102	14,657	3.27	9.33
Nonuniversity diploma or certificate, or some university without degree	3,901	9,708	2.75	7.67	7,209	17,707	3.92	10.50
Bachelor degree, certificate or diploma below bachelor's	5,427	13,664	3.89	10.28	9,479	24,299	5.29	13.72
Postgraduate university degree	7,555	18,261	5.01	12.56	14,934	30,486	7.47	15.81
Weighted average	3,561	9,473	2.49	7.60	6,952	17,424	3.74	10.58

[1] Excludes those who reported zero or negative earnings for the year preceding the census – i.e., 1970 or 1980.

SOURCE Statistics Canada, 1971 and 1981 censuses, special tabulations.

Notes

CHAPTER 1

1 See Economic Council of Canada, *Room for Manoeuvre*, Eighteenth Annual Review (Ottawa: Supply and Services Canada, 1981), Chapter 1.

2 See G. L. Brinkman, *Farm Incomes in Canada*, a study prepared for the Economic Council of Canada and the Institute for Research on Public Policy (Ottawa: Supply and Services Canada, 1981); and J. D. Forbes, R. D. Hughes, and T. K. Warley, *Economic Intervention and Regulation in Canadian Agriculture*, a study prepared for the Economic Council of Canada (Ottawa: Supply and Services Canada, 1982).

3 The number of students enrolled full-time at post-secondary institutions was equivalent to 18 per cent of the total population aged 18 to 24 in 1970-71, compared with 10 per cent in 1960-61.

4 See Economic Council of Canada, *Reforming Regulation* (Ottawa: Supply and Services Canada, 1981).

5 In 1970 total health care costs as a proportion of GNP, as estimated by Health and Welfare Canada, were 7.5 and 7.3 per cent in the United States and Canada, respectively, compared with 8.9 and 7.2 per cent in 1979.

6 Health and Welfare Canada estimates that total health expenditures have risen by about 16 per cent in each of the last three years. They began to increase as a proportion of GNP even before the recession – from 7.5 per cent in 1980 to 7.6 per cent in 1981 and 8.4 per cent in 1982 (the latter two figures being based on preliminary data).

7 The budget surpluses generated in Alberta, Saskatchewan, and British Columbia have tended to be offset by deficits in the other provinces.

CHAPTER 2

1 D. J. Daly, *Canada in an Uncertain World Economic Environment* (Montreal: Institute for Research on Public Policy, 1982), p. 15.

2 J. R. Basche, Jr., *Technology Imports into the United States*, Research Bulletin No. 129 (New York: The Conference Board, 1983), p. 3.

3 See Economic Council of Canada, *The Bottom Line: Technology, Trade and Income Growth* (Ottawa: Supply and Services Canada, 1983), p. 68.

4 Statistics Canada, *Canadian Imports by Domestic and Foreign Controlled Enterprises*, Cat. 67-509 (Ottawa, 1978), p. 18.

5 See, for example, Department of Industry, Trade and Commerce/Regional Economic Expansion, "Foreign-Owned Subsidiaries in Canada 1973-1979," Ottawa, 1983.

6 ECC, *The Bottom Line*, p. 54.

7 IT & C/REE, "Foreign-Owned Subsidiaries."

8 *The Economist*, 25 December 1982, pp. 87-88.

9 Task Force on Trade in Services, "Background Report," Ottawa, October 1982.

10 M. Côté, J. Ratelle, and D. Senik, "The Challenge of the Eighties," A study commissioned by the Alliance of Canadian Travel Associations, SECOR, Inc., Montreal, May 1983, p. 6.

11 *The Economist*, 25 December 1982, p. 83.

12 W. Cline, *Exports of Manufactures from Developing Countries: Performance and Prospects for Market Access* (Washington: The Brookings Institution, 1982).

13 A study along these lines has recently been undertaken by the Institute for Research on Public Policy.

14 *The Economist*, 25 December 1982, p. 84.

15 Morgan Guaranty Trust Company of New York, *World Financial Markets* (June 1983):8-10.

16 *The Economist*, 25 December 1982, p. 93.

17 ECC, *The Bottom Line*, Chapter 9.

CHAPTER 3

1 All the employment and unemployment figures in this section are on a seasonally adjusted basis.

2 Excluding cost-of-living clauses.

3 U.S. Department of Labor, Bureau of Labor Statistics, "International Comparisons of Manufacturing Productivity and Labor Cost Trends: Preliminary Measures for 1982," *News* (May 1983).

4 The National Accounts deficit differs in several ways from other measures, such as the Public Accounts budgetary deficit. The National Accounts deficit is reported on a calendar-year basis and records transactions on an accrual basis rather than a cash basis. Furthermore, the National Accounts accounting framework includes certain revenues and expenditures

that are excluded from the Public Accounts framework, such as the revenues and expenditures associated with the unemployment insurance program and those associated with government pension funds.

Each of these budget or deficit concepts has a specific use. For example, the National Accounts concept is designed to show the impact of government programs on income and activity levels in the personal, business, and foreign sectors of the economy. Because of this, the deficit concept is consistent with the definitions of saving or dissaving in the personal, business, and foreign sectors of the National Accounts accounting framework. The Public Accounts measure is designed to provide Parliament with a means of control over government transactions – including those which do not necessarily have a bearing on the incomes or activities of the personal, business, or foreign sectors – and to facilitate both cash management and financial analysis and planning. It comprises both the administrative budget – the balance of which is frequently referred to as "the budgetary position" – and the so-called "nonbudgetary" transactions, including the net effects of government lending transactions and the operations of various government funds, such as the UI fund and various trust accounts.

With some modifications, the National Accounts presentation incorporates elements of both budgetary and nonbudgetary transactions. The picture is even more complex, however. The actual surplus or deficit of the federal government on a National Accounts basis is affected both by deliberate actions on the part of the government to change fiscal policy (by altering tax rates on the level of expenditures) and by more or less automatic reactions of various tax and expenditure items to changes in the level of economic activity (for example, UI payments) or inflation (for example, interest payments on the public debt). To separate out the discretionary changes from such automatic changes, the government now also provides estimates of what the National Accounts deficit would look like if there were higher average levels of employment or more stable prices.

Details of the various government accounting presentations, together with reconciliation statements, are provided in Department of Finance, *The Federal Deficit in Perspective* (Ottawa, April 1983).

5 For example, see Finance, *The Federal Deficit*; and G. V. Jump, "Interest Rates, Inflation Expectations, and Spurious Elements in Measured Real Income and Savings," *American Economic Review* 70, no. 5 (December 1980).

6 Index-linked bonds such as those issued by the U.K. Treasury provide a means to recycle automatically, in full, the capital repayments incorporated in inflation premiums. The inflation premium is added to the real interest on such bonds, not by paying it out in cash but by writing up, tax-free, the face value of the bonds. The cash interest payment is between 2.5 and 3 per cent of the adjusted face value. Because of this tax-free inflation adjustment, the market value of the bonds tends to equal their growing face value. See "People's Bonds," *The Economist*, 8 August 1981, pp. 64-65; and "The Case for Indexed Bonds," *Business Week*, 19 April 1982, pp. 81-82.

7 Naturally, there would be costs associated with raising the economy to a level of resource utilization that would result in an unemployment rate of 7 per cent, but we have ignored these costs in our calculations.

8 For a detailed description of the methodology, see Economic Council of Canada, *A Climate of Uncertainty*, Seventeenth Annual Review (Ottawa: Supply and Services Canada, 1980), pp. 49-55.

CHAPTER 4

1 Economic Council of Canada, *The Challenge of Growth and Change*, Fifth Annual Review (Ottawa: Queen's Printer, 1968).

2 Employment and Immigration Canada, Strategic Policy and Planning, "UI Exhaustee Study," Ottawa, October 1982.

3 Those benefits include all kinds of payments made under UI regulations.

4 When the unemployment rate is 6 per cent or less, the minimum number of weeks is 14; when the jobless rate is over 9 per cent, it is 10 weeks.

5 These data appear in Employment and Immigration Canada, "Worksharing: A Perspective," Ottawa, March 1983.

6 E & IC, "Worksharing," p. 13.

7 Employment and Immigration Canada, *Unemployment Insurance in the 1980s*, Report of the Task Force on Unemployment Insurance (Ottawa: Supply and Services Canada, 1981), pp. 82-83.

8 E & IC, *Unemployment Insurance*, p. 83.

9 Some provinces (including Quebec) have also developed their own job creation programs.

10 Employment and Immigration Canada, "NEED: New Employment Expansion and Development," Ottawa, June 1983, pp. 1 and 3.

11 Economic Council of Canada, *In Short Supply: Jobs and Skills in the 1980s* (Ottawa: Supply and Services Canada, 1982), pp. 104-107.

12 *The Income Security System in Canada*, Report for the Interprovincial Conference of Ministers Responsible for Social Services (Ottawa: Canadian Intergovernmental Conference Secretariat, 1980); and Statistics Canada, *The Labour Force*, Cat. 71-001, March 1977 to April 1978.

13 E & IC, "UI Exhaustee Study," p. 37.

14 Because welfare programs are run by the provinces (and, in some provinces, by municipalities as well) and are the residual component of the social security system, they reflect all the peculiarities of each province's economic, social, and policy environment. Interprovincial statistical comparison is therefore hazardous at best.

15 Families receiving short-term allowances (which do not include household and clothing allowances) in Alberta

are automatically transferred to the long-term allowance after three months. Also, late in 1982 Alberta doubled to one month (with a possible extension of another month) the length of time that single employable persons could receive welfare benefits.

16 Manitoba's program was not yet in effect. See D. P. Ross, *The Working Poor: Wage Earners and the Failure of Income Security Policies* (Toronto: James Lorimer & Co., 1981), p. 55.

17 Attempts have been made to ease the transition from welfare to paid employment. Ontario, for example, set up the Work Incentive (WIN) program late in 1979, which was aimed not so much at reducing the tax-back rate for persons trying to combine welfare and work income as at encouraging welfare clients to shift over completely to earned income. WIN pays a client who takes a full-time job $250 as a lump-sum payment, as well as a monthly supplement (related to total income and to family size and status) for up to two years, and it provides continuation of the comprehensive family health coverage and the assurance of immediate requalification for provincial assistance if necessary. According to the Ministry, just over 5,000 persons have participated in the program over the past three years, and communication about the scheme to potential users has been a problem. The program at least recognizes, however, that abrupt and complete independence from welfare support is not a viable proposition for many clients, even though they are able and willing to work.

18 A. J. Kahn and S. B. Kamerman, *Income Transfers for Families with Children: An Eight-Country Study* (Philadelphia: Temple University Press, forthcoming).

19 For a discussion of programs in other countries, see S. B. Kamerman and A. J. Kahn, "Income Transfers, Work and the Economic Well-Being of Families with Children: A Comparative Study," *International Social Security Review* (1982):345-82.

20 If, for example, the sole-support mother had earned about $500 more over the year, not only would her Ontario Tax Credit have been reduced and her contributions to unemployment insurance and to the Canada Pension Plan have increased, but her taxable income would have increased sufficiently to cross the income tax threshold. The effective tax rate on her additional earnings, considering all reductions in transfers and increases in taxes and contributions, would have been in the order of 110 per cent. Thus her net income would have decreased.

21 This assumes that the unemployed earner was fully qualified under UI regulations and that the benefit period, including the two-week waiting period, extended over 48 weeks, with the remaining four weeks of the year having been spent on social assistance.

22 See, for example, National Council of Welfare, *Family Allowances for All?*, A report on federal child benefits (Ottawa: NCW, March 1983).

23 P. Burke, C. Casey, and G. Doepner, "Housing Affordability Problems and Housing Need in Canada and the United States: A Comparative Study," Canada Mortgage and Housing Corporation, Ottawa, February 1981; and CMHC, "Background Document on Social Housing," prepared for the All-Sector Housing Conference, Ottawa, 1981.

24 Canada Mortgage and Housing Corporation, *Annual Report 1982* (Ottawa: CMHC, 1983), p. 15.

25 Information about the CMHC's social housing programs is based on data provided by the Corporation's Program Evaluation Division.

26 Of the 144 projects for which information was available, there were 40 (8.4 per cent of all units) in which no family households (for whom this objective had the greatest appeal) received extra subsidy assistance; there were 13 projects (26.9 per cent of all units) where only 1 to 15 per cent of the households were assisted; at the other extreme, there were 23 projects (6.9 per cent of all units) where over 90 per cent of the households were assisted.

27 The oldest program (British Columbia's Shelter Aid for Elderly Renter – SAFER) pays 75 per cent of the amount by which eligible rent exceeds 30 per cent of the family's income up to a maximum – which, for a single person, was $134 per month in July 1982. Over the previous year, single clients had reported an average monthly income of $514, an average rent of $259, and an average SAFER allowance of $63 – giving an adjusted average rent/income ratio of 38 per cent, as opposed to 50 per cent without the allowance.

CHAPTER 5

1 *Opportunity for Choice: A Goal for Women in Canada*, ed. G. Cook, Statistics Canada in association with the C.D. Howe Research Institute (Ottawa: Supply and Services Canada, 1976), p. 2.

2 According to special tabulations provided by the National Council of Welfare.

3 National Day Care Information Centre, *Status of Day Care in Canada, 1980* (Ottawa: Health and Welfare Canada, 1982).

4 "Survey of Child Care," in Statistics Canada, *The Labour Force*, Cat. 71-001, August 1982.

5 Statistics Canada, *A Statistical Portrait of Canadian Higher Education: From the 1960s to the 1980s* (Ottawa: Supply and Services Canada, 1983), p. 26.

6 Z. Zeman, "The Impacts of Computer/Communications on Employment in Canada: An Overview of Current OECD Debates," Institute for Research on Public Policy, Montreal, November 1979.

7 H. Menzies, *Women and the Chip*, Institute for Research on Public Policy case studies of the effects of informatics on employment in Canada (Montreal: IRPP, 1981), p. 75.

8 The disproportionate number of recent labour force entrants among women will tend to widen the earnings gap in both decades, since entrants start at a lower level in the pay scale.

9 National Research Council, Committee on Occupational Classification and Analysis, *Women, Work, and Wages: Equal Pay for Jobs of Equal Value*, ed. D. J. Treiman and H. I. Hartmann (Washington, D.C.: National Academy Press, 1981), p. 33.

10 *Opportunity for Choice*, p. 122.

11 C. Swan, *Women in the Canadian Labour Market*, Task Force on Labour Market Development, Technical Study 36 (Ottawa: Supply and Services Canada, 1981), pp. 79-80.

12 D. C. McKie, B. Prentice, and P. Reed, *Divorce: Law and the Family in Canada*, Statistics Canada (Ottawa: Supply and Services Canada, 1983), p. 225.

13 For information on some of these problems, see Joint Canada Employment and Immigration Commission/Native Women's Association of Canada Working Group on Native Women's Employment, "Native Women: Labour Force Development," A report to the Minister of Employment and Immigration, Ottawa, July 1981.

14 A. J. Siggner, "An Overview of Demographic, Social and Economic Conditions Among Canada's Registered Indian Population," Indian and Northern Affairs Canada, Ottawa, 10 September 1979, p. 21.

15 Indian and Northern Affairs Canada, "A Demographic Profile of Registered Indian Women," Ottawa, October 1979.

16 Indian and Northern Affairs Canada, "Profile."

17 K. Battle, "Some Aspects of the Economic Situation of Canada's Aged," Health and Welfare Canada, *Rapport* 5, no. 3 (December 1982): 1,6-8.

18 Government of Canada, *Better Pensions for Canadians: Focus on Women* (Ottawa: Supply and Services Canada, 1982).

19 As of 30 September 1983, single retirees and families with only one retiree (i.e., with one spouse below age 60) receive a combined monthly GIS/OAS benefit amounting to $514.35, while families with two retirees (where one may be aged between 60 and 64) receive a total monthly benefit of $910.68.

The maximum GIS benefits are paid to persons with little or no earnings. For each dollar of income from other sources over the maximum, benefits are reduced by $0.50 for unattached persons and $0.25 for retirees living as a couple. In addition, six provinces (Nova Scotia, Ontario, Manitoba, Saskatchewan, Alberta, and British Columbia) pay a supplement to GIS recipients.

20 National Action Committee on the Status of Women, "Women and Pensions," A brief prepared for the Pensions Committee, September 1982, p. 3

21 Government of Canada, *Better Pensions*. See also L. Dulude, "Pension Reform with Women in Mind," Canadian Advisory Council on the Status of Women, Ottawa, 1981.

22 Quebec, Saskatchewan (using the concept of similar work), and the federal government have adopted the broader definition.

CHAPTER 6

1 Economic Council of Canada, *Intervention and Efficiency: A Study of Government Credit and Credit Guarantees to the Private Sector* (Ottawa: Supply and Services Canada, 1982), p. 35.

2 ECC, *In Short Supply*, p. 106.

3 Under present tax regulations, families earning less than $26,330 are eligible.

4 NCW, *Family Allowances for All?*, p. 41.

5 ECC, *The Bottom Line*, p. 132.

6 Economic Council of Canada, *Looking Outward: A New Trade Strategy for Canada* (Ottawa: Information Canada, 1975), Chapter 10.

7 External Affairs Canada, *Canadian Trade Policy for the 1980s: A Discussion Paper* (Ottawa: Supply and Services Canada, 1983).

List of Tables and Charts

Tables

1-1 Composition of the Labour Force, by Sex and by Age Group, Canada, 1962, 1972, and 1982 9
1-2 Net Interprovincial Migration, by Province, Canada, 1961-80 9
1-3 Social Assistance Expenditures by Governments, Canada, 1962, 1972, and 1982 11
1-4 Government and the Distribution of Income, Canada, 1961-81 12
2-1 Canada-U.S. Labour Cost Comparisons, 1968-82 20
2-2 Canada-U.S. Intracorporate Trade, Selected Years, 1965-79 23
2-3 Debt Position of the Least-Developed Countries, 1973, 1978, and 1982 30
2-4 Flows of Direct Investment Capital Between Canada and All Countries and Between Canada and the United States, 1974-82 33
3-1 Real Growth in OECD Countries, 1981-83 38
3-2 Selected Economic Indicators, Canada, 1981-83 (Quarterly Figures) 40
3-3 The Effects of Recent Recessions on Selected Labour Factors, Canada, 1975, 1980, and 1982 41
3-4 Changes in the Employment Situation, Canada, 1980-82 41
3-5 External Environment Assumptions (Base Case Projection), 1983-87 44
3-6 Components of the Domestic Crude Petroleum Price to Consumers (Base Case Projection), Canada, 1983-87 45
3-7 The Phasing of Large-Scale Energy Investment Projects (Base Case Projection), 1983-92 46
3-8 Domestic Policy Assumptions in the Base Case 47
3-9 Selected Economic Indicators (Base Case Projection), Canada, 1983-87 48
3-10 Alternative Scenarios for Selected Indicators, 1983-87 50
3-11 Alternative Projections, 1984-87 52
3-12 Inflation Adjustment (on a National Accounts Basis) to Federal Government Budget Balance, 1983-87 55
3-13 Cyclically Adjusted Federal Government Budget Balance, 1984-87 56
3-14 Projected Impact of Fiscal Policy Initiatives, 1984-87 58
4-1 Distribution of Husband-and-Wife Census Families (with the Husband Aged Less than 65), by Employment and Unemployment Characteristics, Canada, 1971 and 1979 60

4-2 Unemployment Insurance Beneficiaries in January, by Age and Sex, Canada, 1981-83 61
4-3 Average Weekly Insurable Earnings in January of Beneficiaries Receiving Regular UI Benefits with No Earnings Reported, by Sex, Canada, 1981-83 61
4-4 Distribution of Beneficiaries Receiving Regular UI Benefits in January, by Weeks of Insurable Employment, Canada, 1981-83 62
4-5 Job Creation and Training Programs: Numbers of Participants and Costs, Canada, 1977-83 64
4-6 Approximate Retention Schedule for Employable General Welfare Assistance Cases, Metropolitan Toronto 66
4-7 Distribution of General Welfare Assistance Caseload in November, Metropolitan Toronto, 1980-82 67
4-8 Disposable Income for a Family of Four, by Work Status and by Province, Canada, 1979-80 69
4-9 Family Net Income as a Proportion of the Average Production Worker's Net Income, and Canada's Ranking among Nine Jurisdictions, by Family Type 71
4-10 Core Income Transfer Programs, Eight Countries 72
4-11 Distribution of Rental Households and Incidence of Housing Need, by Category, Canada, 1980 and 1982 75
4-12 Distribution of Rental Households with Core Housing Need and CMHC Social Housing Commitments, Canada, by Region, 1950-82 75
4-13 CMHC Subsidy Expenditures on Social Housing, by Program Area, Canada, 1973-82 78
4-14 Provincial Shelter Allowance Programs, Canada, 1981 79
5-1 Female Participation Rates in Nine Industrialized Countries, 1960, 1970, and 1981 82
5-2 Average Contribution of Women in the Labour Market to Family Earnings in Two-Parent Families, by Family Status, Canada, 1971, 1975, and 1979 82
5-3 Female Participation Rates in Nine Industrialized Countries, by Age Group, 1981 83
5-4 Average Hourly Wage of Women and Men, by Time Worked and by Union Membership, Canada, 1981 87
5-5 Numbers and Average Annual Earnings of Women and Men in the Twenty Highest-Paid Occupations, Canada, 1970-71 and 1980-81 88
5-6 Numbers and Average Annual Earnings of Women and Men in the Twenty Lowest-Paid Occupations, Canada, 1970-71 and 1980-81 89
5-7 Income of Economic Families with Head Aged 65 and Over, by Family Status, Canada, 1971 and 1981 92
A-1 Public Health Care Coverage and Costs in Ten OECD Countries, 1960, 1980, and 1981 113
A-2 Real Growth in Seven OECD Countries, 1981-83 113
A-3 Consumer Price Index in Seven OECD Countries, 1981-83 114
A-4 Rate of Unemployment in Seven OECD Countries, 1981-83 114
A-5 General Government Financial Balances, Seven OECD Countries, 1979-82 115

A-6 Current Account Balance as a Proportion of GNP in Seven OECD Countries, by Quarter, 1981-82 115

A-7 Gross Annual Commitments of Differential Interest Contributions by CMHC under Section 56.1 of the National Housing Act, by Province or Territory, 1978-82 116

A-8 Participation Rates of Women and Men, by Age Group, Canada, 1971 and 1981 116

A-9 Participation Rates of Women and Men, by Educational Attainment, Canada, 1971 and 1981 116

A-10 Participation Rates of Women and Men, by Family Status, Canada, 1971 and 1981 117

A-11 Distribution of Preschool Children Whose Parents Would Prefer to Change Care Arrangements, by Mother's Age, Canada, February 1981 117

A-12 Distribution and Proportion of Full-Time Female University Students, by Specialization, Canada, 1972-73 and 1981-82 118

A-13 Average Annual and Hourly Earnings of Women and Men, by Educational Attainment, Canada, 1970 and 1980 118

Charts

1-1 Annual Growth Rate of Real GNE, Canada, 1962-82 5

1-2 Annual Growth Rate of the Consumer Price Index, Canada, 1962-82 5

1-3 The Unemployment Rate, Canada, 1962-82 5

1-4 Annual Growth Rate of Productivity in Commercial Industries, Canada, 1962-82 6

1-5 Population Growth, Canada, 1961-81 7

1-6 Age Distribution of the Population, Canada, 1961, 1971, and 1981 7

1-7 Labour Force Participation Rates, by Sex and Age Group, Canada, 1961-82 8

1-8 Average Household Income in Constant (1980) Dollars, Canada, by Province, 1970 and 1980 10

1-9 Consolidated Government Expenditures as a Proportion of GNP, by Component, 1965-80 13

1-10 Gross Debt of the Federal Government as a Proportion of GNP, Canada, 1962-81 14

2-1 Distribution of Exports and Imports, by Commodity Group, Canada, 1960, 1970, and 1980 19

2-2 Distribution of Exports by Destination and Imports by Origin, Canada, 1960 and 1982 24

3-1 Composition of Unemployment by Demographic Group, Canada, 1980-83 42

4-1 Metropolitan Toronto General Welfare Assistance Caseload, January 1976-May 1983 66

4-2 Family Units Experiencing Unemployment and the Social-Assistance Caseload, Selected Provinces, January 1981-May 1983 68

4-3 CMHC Commitments for Social Housing: Number of Units and Capital for Loans and Investment, 1973-82 76

4-4 Distribution of CMHC Commitments for Social Housing, by Type of Program, 1973-78 and 1978-81 77

5-1 Distribution of Full-Time University Students by Sex, by Level of Study, Canada, 1972-73 and 1981-82 85
5-2 Change in Average Annual Earnings of Women and Men, by Age Group, Canada, 1970-80 86
5-3 Average Income of Non-Native and Native Families with Dependants, Rural and Urban, Canada, 1980 91

Project Staff

Research

R. A. Jenness, Director
J.-A. Boulet
L. Buchanan
E. Cloutier
P. de Broucker
P. Gorecki
R. Hirshhorn
L. Lavallée
R. A. Matthews

CANDIDE

R. S. Preston, Director
B. J. Cain
F. Delorme
S. F. Gilby
B. K. Lodh
P. E. Nevin
P. S. Rao
H. S. Saiyed
M. E. Willis

Thanks are also due to Fran Peake and Mary Rowe, secretaries, and to various support groups at the Council, in particular the Statistical Services, the Word Processing Unit, the Communications Division (including the Translation Section), and the Registry Service, for their contribution to this report.